FARMER MAC

# DAVE'S GPS

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**<u>Reflections from the Heartland</u>**

By Dr. David M. Kohl

Omaha! Omaha! No, this is not an article about an audible call at the line of scrimmage by Peyton Manning, the Denver Broncos quarterback. It was the Super Bowl of lifelong learning at the National Agricultural Bankers Conference in the heartland of America, Omaha, Nebraska. Approximately 750 attendees, the largest in two decades, from over 40 states, Washington, D.C., four Canadian provinces, and Turkey were in attendance to recharge their batteries. The conference was organized by the visionary director, John Blanchfield, and his team from the American Bankers Association. This was my 37th consecutive conference. This year's event was chock-full of educational sessions and hosted a record number of exhibitors serving agriculture and rural America. Let's draw upon a few points and perspectives from this stellar event.

The theme of Sunday's preconference event co-sponsored by FINPACK and Farmer Mac was "Turbulent Times Require Better Data." It was interesting how both sponsors illustrated how they were utilizing data and benchmarks to allow lenders to analyze risk and position themselves to better educate their customers. There was no doubt from this session that while farm equity is strong, profits, cash flow, and financial liquidity will be a focus particularly in the grain industry. Both the sponsoring organizations are strategically positioning to proactively utilize information and data to identify risk through shock testing and volatility analysis. Of course, I focused on taking big data to small data, in other words, making it into useful information by creating financial dashboards with key ratios and metrics.

The conference kickoff speaker was renowned futurist Dr. Lowell Catlett, Dean of the College of Agricultural, Consumer and Environmental Sciences at New Mexico State University. Both of us quickly reminisced about serving as state and national FFA officers after his talk on "big data," the theme of the conference. The key takeaway was that it's all about "N-1." That is, no matter how much data one has, it is about customizing data to the individual to provide a unique customer experience. Interestingly enough, those in the baby boomer generation got their first job at approximately 12 years of age; however, Dr. Catlett said individuals in the millennial generation are first employed at the average age of 22. He stressed that as more big data is used, the importance of social connection and personality skills will rise to the top. Big data and technology will reinvent education and flip the classroom. Instead of lecture in class and then homework, the majority of lecture will be online outside the classroom and applications of the content will be facilitated using a face-to-face component. He presented an example illustrating doctors who spend three minutes and 20 seconds extra with their patients are less likely to be sued. This shows the importance of bedside manner as another example of human skills.

The luncheon speaker, Harry Stine, illustrated how a handicapped individual who is dyslexic and autistic can become a billionaire by listening as he developed a seed and plant breeding process. In the afternoon, there was a good discussion on how banks are cultivating the next generation of farmers and bankers. More lending institutions and agribusinesses are providing educational experiences for young producers and those in transition and growth. Government programs including crop insurance and risk coverage will be very critical with a five-year commitment that was presented by Drs. Hart, Schnitkey and Watts from the land grant institutions in Iowa, Illinois, and Montana.

The commodity sessions at the crack of dawn provided some interesting perspectives. Beef and livestock markets are positioned be strong for the near future while there may be modest declines in dairy according to Dr. Brester of Montana State University and Dr. Mozic of University of Minnesota, respectively. Grain may be settling in for a moderate to long-term downturn in the cycle depending on supply and demand levels.

Dr. Jason Henderson of Purdue University and Dr. Brent Gloy, professor turned farmer in Nebraska, provided plenty of food for thought. Who is at risk in the current economic environment? Young and beginning farmers who purchased a considerable amount of land, machinery, or encumbered many acres with high cash rents may struggle. Another risk they identified was rural Main Street. They indicated it was important to watch for outside investors in agriculture because they often will dictate the direction of land values according to their relative activity in the marketplace.

My good friend Dr. Ed Siefried indicated that the reduction in the Federal Reserve's balance sheet and increase in interest rates was a certainty. Up to 40 percent of grain prices and capitalization of land values can be attributed to low interest rates and low value of the dollar, which resulted in the ability to export agricultural commodities during the commodity super cycle.

A session that really generated much attention was the "alpha pup" panel which contained a group of young agriculture producers who are millennials less than 34 years of age. Interestingly enough, all individuals on the panel, while utilizing technology, still preferred face-to-face communication with their lenders. Management practices ranged from one individual spending most of his time monitoring business activities from his office, to another engaged in outside the farm investments, to a "start from scratch" producer, to one who is involved in a complex family farming business. This panel gave attendees food for thought concerning strategies to accommodate this new generation of producers who will be thought leaders of the industry.

On the final day, Chuck Cruickshank addressed the topic of sustainability in agriculture. His point was that the U.S. and global consumers are increasingly demanding their products be from farmers practicing sustainable and humane policies, and every farmer needs to be aware of this.

I addressed the conference for my 37th year on the final day. I called a Peyton Manning audible and basically did a wrap up of the conference, recognizing first year attendees up to the person with the longest tenure, Frank Bruning, whose first conference was in 1963 in Kansas City, where the 2015 conference will be held next October.

**Lender Tip: Conference Report**
This article was written as a wrap of the conference with the assistance of three attendees from the First Bank and Trust Co. of Abingdon, Virginia. Paula Martin, Micah Owens, and Raleigh Hayter each provided me a summary of the conference as a best management practice of the bank for individuals attending conferences. Hopefully, other institutions will consider this practice to help educate their staff. These trainees get an A+ from the professor for their diligent work!

Global Economics

A quick trip across the ocean to Europe finds that an economic slowdown is in progress. The purchasing manager indices throughout the major European economies are predicting a slowdown of growth. Any adverse political or economic event could place the euro area, which is 25 percent of the world economy, into recession. Deflation in the region and central bank stimulus are two key factors that need close attention. Reduced oil prices have Mr. Putin scrambling with austerity strategies throughout Russia. Will he resort to aggressive political or military strategies to counter Western sanctions and will he direct a closer alliance with China for support?

Speaking of China, recent economic stimulus by the government would suggest concern of an economic slowdown by the central planners. Economic growth has slowed particularly in housing and infrastructure, which are areas of the economy that fueled growth. Retail sales are down 20 percent year over year for this second largest economy in the world. Other areas of the world including Brazil and Argentina are either in recession or on the brink of recession.

Domestic Economics

Examination of key economic indicators finds the U.S. economy is the strongest in the world at this period of time. The leading economic index (LEI) and purchasing manager index (PMI) suggest a bullish economy for the next six months. Reduction of oil prices may provide a boost to the economy during the holidays and beyond.

The unemployment rate is currently 5.8 percent, and 11.4 percent when including discouraged and displaced workers (U-6). This would suggest the Federal Reserve may consider raising rates particularly if wages start to increase.

Housing starts are at approximately one million annually, which is adequate but not robust. This factor is critical for the sustainability and growth of the U.S. economy. Factory utilization, a driver of U.S. economics, is up, but will it be impacted as the global economy starts to soften? This will be a critical factor to examine particularly given its importance to many rural areas.

Core and headline inflation are 1.7 percent and 1.3 percent respectively, which is one of the main reasons the Federal Reserve has not raised interest rates. A surprise has been the growth of the U.S. economy, which came in at 3.9 percent for the third quarter. This is quite robust and it will be interesting to observe as it carries over into 2015.

Two observations concerning the domestic and global economies relate to copper and oil. Copper prices are now in the high two dollar range. This raises concern about the depth and breadth of possible global economic slowdown because copper is used in many products and is usually a lead indicator of economic health. Also, reduction in oil prices may be a method to place pressure on Russia and Mr. Putin and other dictators in oil producing nations. Will this in turn create geopolitical or military risk in very fragile economies in the world? How will it impact U.S. energy production? If oil stays near $50 per barrel, it could have an interesting impact on the economies of Ohio, Pennsylvania, and North Dakota. Only time will tell how this volatility will play out.

**Lender and Business Dashboard Economic Indicators** (for the month of November)

| Indicator | Current | Green | Yellow | Red |
|---|---|---|---|---|
| **Leading Economic Index - LEI** | 105.5 | ✓ | | |
| **LEI Diffusion Index** | 80% | ✓ | | |
| **Purchasing Manager Index - PMI** | 58.7 | ✓ | | |
| **Housing Starts (millions)** | 1.028 | | ✓ | |
| **Factory Capacity Utilization** | 80.1 | ✓ | | |
| **Unemployment Rate** | 5.8% | ✓ | | |
| **Core Inflation** | 1.7 | ✓ | | |
| **Headline Inflation** | 1.3 | ✓ | | |
| **Oil Price ($/barrel)** | $70.08 | | ✓ | |
| **Yield Curve** | 2.14 | ✓ | | |

**Lender and Business Dashboard Economic Indicator Benchmarks**

| Indicator | Green | Yellow | Red |
|---|---|---|---|
| **The Conference Board Leading Economic Index® - LEI** | **Increasing** | **Flat to Decline** | **Decline 0.3% for 3 consecutive months AND >1% over the period** |
| **LEI Diffusion[1]** | **>60%** | **40%-60%** | **<40%** |
| **Purchasing Manager Index - PMI** | **>50** | **41.7-50** | **<41.7** |
| **Housing Starts (millions)** | **>1.5** | **1.0-1.5** | **<1.0** |
| **Factory Capacity Utilization** | **>80%** | **70%-80%** | **<70%** |
| **Unemployment Rate** | **5%-6%** | **6%-8%** | **>8% or <5%** |
| **Core Inflation** | **0%-2%** | **2%-4%** | **>4% or <0%** |
| **Headline Inflation[2]** | **0%-4%** | **4%-5%** | **>5% or <0%** |
| **Oil Price[3] ($/barrel)** | **<$50** | **$50-$100** | **>$100** |
| **Yield Curve[4]** | **Steep** | **Flattening** | **Inverted** |

[1]Ten indicators make up the LEI - measures % that are increasing; [2]Includes food & energy;
[3]Consumer's perspective; [4]3-Month Treasury Bill rate to 10-Year Bond rate