Should Surging Fertilizer Costs Worry CFIs?

by Steve Brown

Summary: As farmers enter planting season, they are faced with surging fertilizer prices. Prices are expected to increase 80% YoY, which affects 15% of their total costs. We dig deeper into what this means for farmers with different crops and how they can weather this type of hefty increase, so that you know how to best support them.

There were 588 hours of sunshine in the spring of 1948. This was the highest number ever recorded. The spring of 2014 was also quite sunny with 306 hours, while the least sunny spring on record is 1963 with only 82 hours. While we don't know yet how many spring sunshine hours 2022 will bring, many of us enjoy our sunny days.

Farmers likely enjoy sunny days too, as they start the spring planting season. Yet, this year, they're facing huge increases in fertilizer prices. These are forecast to be as much as 80% higher YoY, according to a study from Texas A&M University's Agricultural and Food Policy Center.

That hike represents both an opportunity and a risk for community financial institutions (CFIs) that support these customers. On the plus side, farmers may have higher loan needs in order to pay for fertilizer. But, there is also a risk that fertilizer prices could make loan repayment more difficult for farmers. Or farmers might economize by using less fertilizer and, therefore, have lower crop yields and reduced revenue. We explore this area a bit deeper to provide some insight.

Fertilizer could go from 15% to 27% of a farm's cash outlay

Fertilizer typically consumes about 15% of a farmer's total cash outlay in a growing season. With the 80% increase, that number could rise to 27% of their total budget. According to the study, a farm growing feed grain might pay $128K more this year than last, which equates to nearly $40 an acre more. Rice growers are set for the hardest hit: an increase of just over $62 an acre. Cotton farms are looking at a bump of just under $30 per acre or $114K for the average cotton grower. "*Our fertilizer bill has more than doubled,*" says Chris Edgington, who is president of the National Corn Growers Association and farms about 4K acres in northern Iowa.

Energy costs and supply chain issues among reasons for price hike

A variety of reasons are behind the explosion in fertilizer prices. Raw materials are all substantially more expensive, with ammonia up 210% from September 2020, liquid nitrogen up 159%, urea 115% higher, MAP up 125%, DAP more than doubled in price, and potash up 134%. Those increases reflect pandemic-related supply chain issues, as well as China's decision to stop exporting phosphate and planned sanctions against Belarus, which exports potash.

The rise in oil and gas prices is an issue too. Mining and manufacturing fertilizer and its components are both energy-intensive, and energy costs are also substantially higher, a reflection of the uncertainty around whether Russian oil and gas will be available on the world market in the coming months.

How farmers can weather the increase

The USDA predicts that fertilizer prices will push net farm income slightly lower in 2022, dropping by 4.5%. Even so, farmers have options that may help them minimize the impact.

From a position of strength. Many farmers are approaching this year from a position of strength. Last summer's crop was robust and fetched similarly healthy prices. Corn prices were up more than 30% in 2021 and total farm income rose 23% over 2020 to $117B, which is the highest total in 8Ys.

With more credit. Because of these factors, credit quality is strong for the agriculture industry as a whole. Farm loans totaled $177B in Q3 2021 and just 1.4% of agriculture loans were 30 days or more past due, the lowest figure since 2015. Many farmers can handle more debt than they had at the end of last year.

By testing the soil. Because unused fertilizer stays in the soil from year to year, some farms may have holdover nutrients from last year. Sampling levels of nitrogen and other crucial plant minerals already in the fields may help farmers calculate lower fertilizer needs. This could also provide an opportunity to grow other, cheaper crops than more fertilizer-hungry ones.

By using forward contract pricing. Farmers also have the option of locking in favorable commodities pricing on at least some of what they grow through forward contracts. Crop prices aren't up by as much as fertilizer, but many crops are still bringing in good prices. Forward contracts can help farmers hedge against the possibility that those prices will drop.

While fertilizer prices are surging, there are options for farmers to mitigate this increase. Discussing these options with your customers and supporting them through this situation will enable both you and your customers to thrive, despite this current challenge.

COMMERCIAL LOAN GROWTH AND FLOATING RATE ASSETS

Does your institution need fully-funded, senior secured floating-rate loans to diversify your portfolio? Learn about our C&I Loan Program to meet your loan growth objectives.

ECONOMY & RATES

Rates As Of: 04/01/2022 06:50AM (GMT-0700)

Treasury	Yields	MTD Chg	YTD Chg
3M	0.52	0.17	0.46
6M	1.06	0.37	0.87
1Y	1.73	0.11	1.35
2Y	2.45	0.11	1.71
5Y	2.58	0.11	1.31
10Y	2.45	0.10	0.93
30Y	2.53	0.08	0.63

FF Market	FF Disc	IOER (Interest on Excess Reserves)
0.33	0.50	0.40
SOFR	**Prime**	**OBFR (Overnight Bank Funding Rate)**
0.29	3.50	0.32