



California Drought in 2015 and its Economic Impact on Agriculture

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Introduction

California is now heading into its fourth year of severe drought. All Californians face significant water restrictions during 2015. For urbanites, the restrictions will represent an inconvenience, including brown lawns and empty swimming pools. For growers, ranchers, and agribusinesses, the restrictions pose a threat to their livelihoods. The primary purpose of this report is to assess the drought's potential economic impact on California's agriculture sector.

Following are our four key takeaways:

- The damages wrought by the drought in 2015 will be worse than those in the previous year, but far from catastrophic. With each successive year of drought, the underground water tables decline further, boosting the cost of pumping groundwater to the surface and increasing the likelihood of well failure.
- Not all commodities will be impacted equally. Those yielding the highest returns on investment will be affected least by the drought because growers will redirect the limited water supply to these plants and away from those yielding the lowest returns. California's highest yielding crops are its permanent plantings, including nuts, citrus and other tree fruits, and vine-grown fruits and vegetables.
- Growers will again fallow some of their land and redirect the water that would have been used to irrigate those acres toward more profitable crops grown in other fields. They are expected to fallow 550,000 to 600,000 acres this year, about 6-7 percent of total irrigated acreage and 30 percent more than they fallowed in 2014. The resulting losses in revenue will fall most heavily on field crops such as corn, wheat, cotton, rice, hay, pasture, and beans.
- Agriculture lenders will experience some deterioration in the credit quality of their California-based borrowers, but it will be modest in scope. The borrowers connected with the permanent-plantings will be least affected, whereas those connected with field crops and dairy production will bear the brunt of the continuing drought.

Our bottom line conclusion is that most California-based growers, ranchers, and agribusinesses will remain in the black in 2015, albeit with a few outliers posting modest losses and slight deteriorations in credit quality; but their financial stress will worsen if the drought persists into 2016. This is much the same conclusion that we reached last year at this time in assessing the drought damages in 2014.