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FEDERAL RESERVE BANK OF CHICAGO

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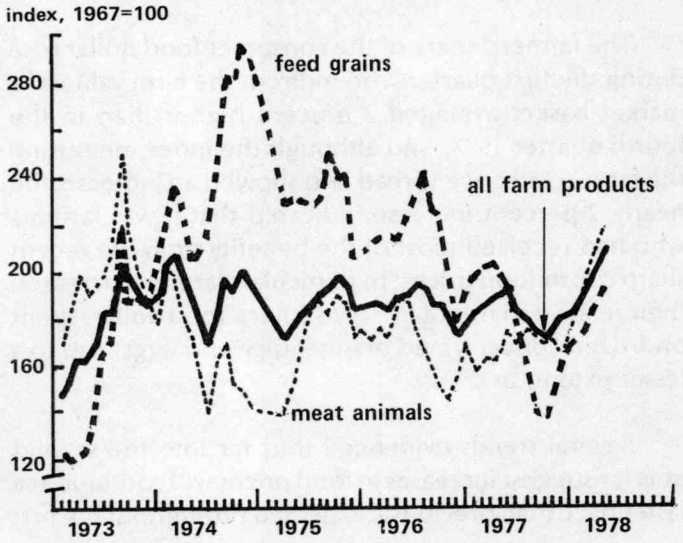
Division of Agricultural Economics

FARM INCOME PROSPECTS for 1978 have improved considerably in the past few months. Less-than-expected production and strong consumer demand have substantially boosted prices and potential earnings for livestock producers. Prospective earnings of crop farmers have also been revised upward from the dismal concensus of a few months ago, reflecting larger benefits from government programs and firmer prices because of the Southern Hemisphere drought and strong export markets. In line with these developments, the USDA now forecasts that net realized farm income will approximate $24 billion in 1978. Earlier forecasts had been for a slight decline from last year's level of $20.4 billion.

The upturn in farm prices mirrors the more optimistic outlook for farm earnings. In mid-April the index of prices received by farmers was at the third highest level on record—20 percent above last September's low. For the first four months of this year, the index averaged 5 percent above the same period a year ago. The index of prices paid by farmers for production items averaged only 4 percent higher. District farmers have benefited particularly from the marked rise in commodity prices over the past few months. For example, the index of prices received for meat animals in mid-April was up 28 percent from last September and 32 percent higher than a year ago. Moreover, prices for corn and soybeans were up 40 and 30 percent from their respective lows of last September.

Farm prices up sharply from September 1977 low



Corn and soybean prices still lagged year-earlier levels in April. However, there is growing evidence that corn prices this summer will not duplicate the plunge of last year and for all of 1978 may exceed last year's $2.03 per bushel average by a considerable margin. Soybean prices will come closer than previously expected to the record monthly average of $6.82 per bushel received in 1977. Along with the upturn in wheat prices and prospects for continued high livestock prices, it appears the average index of prices received by farmers will reach a new high in 1978, perhaps more than a tenth higher than last year.

Cash receipts of livestock producers have shown the strongest gains from the recent upswing in commodity prices, a trend that will no doubt prevail throughout the year. Receipts from cattle and calf marketings—which in recent years have accounted for close to 45 percent of all livestock receipts—may rise by a fourth because of higher prices. And higher prices for milk and hogs, coupled with larger poultry production, point to substantial gains in receipts for almost every component in the livestock complex. Although a number of uncertainties still prevail about developments during the rest of the year, it appears that livestock receipts in 1978 may be up 15 to 20 percent from last year's $47.4 billion.

Crop receipts—which include net loans to farmers from the Commodity Credit Corporation—totaled $47.6 billion in 1977. In addition, crop farmers received the bulk of the $1.8 billion in government payments to farmers in 1977. During the first few months of 1978, crop receipts were down slightly from a year ago, but a large rise in government payments was more than offsetting. At this juncture, there are a number of pitfalls in projecting what combination of receipts and government payments crop farmers might receive during the rest of

the year. These pitfalls are related mostly to uncertainties regarding the level of farmer participation in the long-term grain reserve and the feed grain program. Another major pitfall is related to the highly uncertain 1978 crop prospects that have been accentuated this year by a late planting season. Developments in these areas will have an important bearing on the distribution of market receipts, deficiency, diversion, and disaster payments, and CCC loans received by crop farmers during the remainder of the year.

Despite these uncertainties, there are some encouraging signs that the combined total of crop receipts and government payments to farmers might be up about 5 percent in 1978. Export markets continue strong, which will help support crop prices this summer. The legislation signed this week that was used to boost the wheat target price from $3.05 to $3.40 per bushel portends a large deficiency payment to wheat producers again this fall. Evidence that feed grain farmers will join wheat producers in heavy participation in the long-term grain reserve is just beginning to mount. Heavy participation in the grain reserve, on the one hand, implies large government storage payments. At the same time, the more grain that enters the reserve the more free market supplies will tighten tending to support grain prices—and hence receipts—at higher levels. And finally, the late planting season increases the likelihood of farmer participation in the feed grain program. Greater participation in the feed grain program would result in larger land diversion payments, increased eligibility for CCC loans, and—if relevant—larger government deficiency and disaster payments. Simultaneously, greater participation in the feed grain program, coupled with the increased yield risks from a late-planting season would tend to support crop prices and receipts because of the implications for somewhat less production.

Production costs are also expected to be up considerably this year. Feed costs will probably rise because of larger purchases. Expenses for livestock purchases will be sharply higher, as suggested by the nearly 30 percent year-to-year rise in feeder stock prices in April. Although prices are unchanged from a year ago, the total fertilizer bill may be up this year because more will be purchased during the spring peak in prices. Among other major cost accounts, increases will likely be evident in interest expenses, depreciation, repairs, and hired labor.

On balance, the farm earnings picture looks materially brighter than a few short months ago. Although conditions could still depart sharply from the recent trends, it appears that net realized farm income for 1978 might even exceed the USDA's current estimate of $24 billion by about $1 billion. The stronger earnings would go a long way toward alleviating many of the concerns so widespread a short time ago.

Gary L. Benjamin
Agricultural Economist

RETAIL FOOD PRICES have risen sharply in recent months, partly in response to higher incomes and record employment. Demand for most foods has been bolstered. Reduced supplies of some food groups—red meats and fresh fruit in particular—have also contributed to the price rise. The March index of retail prices of foods eaten at home was 4 percent higher than at the beginning of 1978 and 8 percent higher than a year earlier. Although the increase is expected to slow during the second half, the USDA has raised its earlier estimate and now expects 1978 grocery store food prices to average 6 to 8 percent higher than last year.

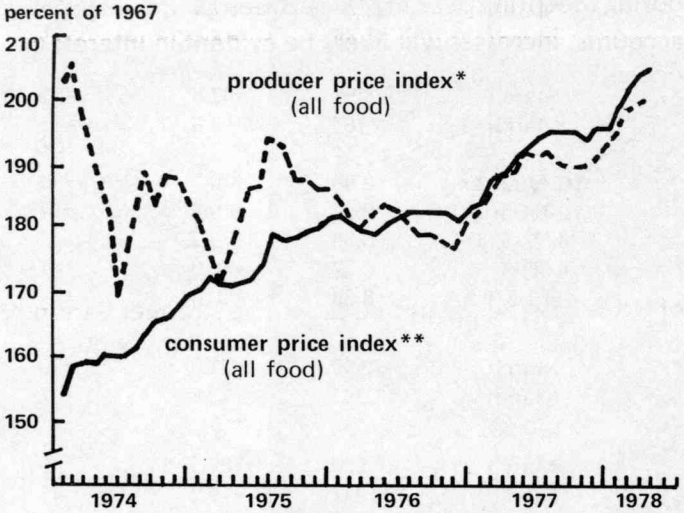
Several developments contributed to the unexpected strength in food prices during the first quarter. As recently as December, most observers were expecting that a sizable increase in pork production during the first three months of the year would tend to reduce pork prices as well as any beef price increases that might follow the expected reduction in beef supplies. Pork production did not increase to the extent expected, however, and the reduction in beef supplies may have been more than many observers expected. Smaller supplies of both fresh and processed fruit contributed to a marked rise in citrus and noncitrus fruit prices in the first quarter. Average sugar prices were up, due largely no doubt to the new support program legislated last fall. Weather-related transportation difficulties interfered with normal marketings in some areas, further aggravating the situation.

The farmers' share of the consumer food dollar rose during the first quarter. The index of the farm value of a market basket averaged 7 percent higher than in the fourth quarter 1977. And although the index measuring the farm-retail price spread also showed an increase, the nearly 2 percent increase indicated that it was farmers who had received most of the benefits from the recent sharp rise in food prices. In particular, farmers increased their relative shares of the consumers' food dollars spent on frozen concentrated orange juice and eggs, and to a lesser extent, beef.

Several trends evidenced thus far into the second quarter suggest increases in food prices will continue at a faster pace than previously expected throughout the first

half of the year. Increased dairy support prices went into effect April 1, resulting in higher prices to consumers for milk and other dairy products. With hog prices continuing to exceed expectations, they have not yet provided enough restraint on retail beef prices to keep them from rising to record levels. Heavy rains in central California in March and April disrupted the normal planting and harvesting of several types of fresh vegetables, resulting, for example, in sharp increases in lettuce prices. Lettuce prices, however, are expected to return to more normal levels by June as new crops are harvested.

First quarter 1978 food prices rise sharply



*Formerly called wholesale price index.
**After January 1978 index is for all urban consumers.

The outlook for food prices in coming months suggests a general slowing from the increases in recent months. Poultry and pork supplies are expected to increase in the second half, and this should have a moderating effect on retail beef prices. But the USDA's projection of a 5 to 6 percent reduction in second-half beef supplies could combine with the greater affluence of consumers to hold prices at least near their current levels, boosting average retail beef prices for the year to a record level. Coffee prices throughout 1978 should average well below last year's level. Although other food imports will probably continue higher throughout the year, they are not expected to be the significant factor behind higher grocery store food prices that they were a year ago.

The strong demand observed for food in recent months, fueled by higher real disposable per capita incomes, is generally expected to taper off and fall more in line with the demand conditions for the remainder of the economy. The surprising strength in first-quarter food prices caused the USDA to boost its estimate of the year-to-year gain to a range of 6 to 8 percent. Although it is anticipated that farmers will be less of a factor behind second-half food price increases than they were in the first half, higher charges are probable for assembling, processing, transporting, and distributing a market basket of foods. It is therefore possible that 1978 food price gains could exceed the current USDA estimate.

Don A. Langford
Agricultural Economist

Selected agricultural economic developments

Farm finance					
Total deposits at agricultural banks†	1972-73=100	April	179	+ 1.9	n.a.
Time deposits	1972-73=100	April	209	+ 1.9	n.a.
Demand deposits	1972-73=100	April	130	+ 2.0	n.a.
Total loans at agricultural banks†	1972-73=100	April	209	+ 0.7	n.a.
Production credit associations					
Loans outstanding					
United States	mil. dol.	March	13,427	+ 1.2	+ 7
Seventh District states	mil. dol.	March	2,648	+ 1.2	+11
Loans made					
United States	mil. dol.	March	2,414	+26.3	+10
Seventh District states	mil. dol.	March	593	+24.3	+14
Federal land banks					
Loans outstanding					
United States	mil. dol.	March	22,234	+ 1.5	+15
Seventh District states	mil. dol.	March	4,604	+ 2.8	+21
New money loaned					
United States	mil. dol.	March	491	+42.8	–11
Seventh District states	mil. dol.	March	167	+98.8	–16
Interest rates					
Feeder cattle loans††	percent	1st Quarter	8.88	+ 0.7	+ 2
Farm real estate loans††	percent	1st Quarter	9.04	+ 0.6	+ 1
Three-month Treasury bills	percent	4/27-5/3	6.38	– 0.2	+37
Federal funds rate	percent	4/27-5/3	7.27	+ 6.0	+41
Government bonds *(long-term)*	percent	5/1-5/6	8.38	+ 0.8	+ 8
Agricultural trade					
Agricultural exports	mil. dol.	March	2,519	+21.8	+10
Agricultural imports	mil. dol.	March	1,391	+13.8	+ 7
Farm machinery sales					
Farm tractors	units	March	14,580	+89.1	– 6
Combines	units	March	917	+ 9.2	–16
Balers	units	March	633	+62.7	–44

†Member banks in Seventh District having a large proportion of agricultural loans in towns of less than 15,000 population.

††Average of rates reported by District agricultural banks.

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