FEDERAL RESERVE BANK OF CHICAGO

AGRICULTURAL LETTER

ISSN 0002 - 1512

May 18, 1979 | Number 1499

AGRICULTURAL CREDIT CONDITIONS among rural banks in the Seventh District were characterized by stronger loan demand, tighter liquidity pressures, and higher interest rates on farm loans. These trends represent the consensus view of the more than 580 agricultural bankers that responded to an April survey. The indication of tigher credit conditions was somewhat surprising in light of the strong farm earnings in recent months. Preliminary USDA estimates show that net farm income exceeded $33 billion (seasonally adjusted annual rate) in the first quarter, up from $26 billion in the same period a year ago and one of the highest quarters on record. But crop farmers did not share proportionately in the earnings with livestock and dairy producers. And sharply rising input prices, coupled with expanded purchases by farmers, may account for the tightening credit conditions.

The index of farm loan demand registered an unusually large rise in the first quarter, moving slightly ahead of the year-ago level (see table on page 2). This follows indications late last year that farm loan demand was easing. However, increased capital expenditures, a sharp expansion in pork production, and higher input prices apparently strengthened farmers' borrowing needs. Purchases of farm machinery and equipment were strong in the first quarter, as evidenced by preliminary estimates that show a 12 percent year-to-year rise in unit retail sales of farm tractors and a 17 percent rise in combine sales. Available evidence suggests hog producers in district states increased winter farrowings by 15 percent and were gearing up for an even larger increase in spring farrowings. And sharply higher prices paid by farmers for feeder cattle, fuel, and other inputs added to farmers' loan demand.

Evidence of a strong farm loan demand is also reflected in data from production credit associations, the chief competitors to banks for nonreal estate farm loans. During the first quarter, money loaned to farmers in district states by PCAs exceeded the sluggish performance of a year earlier by nearly a fourth.

Farm loan repayment rates apparently slowed somewhat in the first quarter, interrupting the steady uptrend that had been evident since the third quarter of 1977. Similarly, renewals and extensions of farm loans were up somewhat. While these observations could reflect cash flow pressures on some farmers, a more general explanation might be tied to the strong loan demand and the rising interest rates on farm loans. In line with increases in farm credit needs and interest rates on farm loans, farmers may have been reluctant to pay off loans previously acquired at lower rates of interest.

Interest rates charged by banks on farm loans rose sharply again in the first quarter. The average of rates reported for feeder cattle loans approximated 10.5 percent, as did the average for operating loans and farm real estate loans. These higher levels reflect an increase of about 1 percentage point in the past six months and an increase of 1.5 percentage points from a year ago. Such rapid increases in farm loan interest rates, although modest compared with the variability sometimes evident in money market rates of interest, are very unusual for banks. Several factors have contributed to the rise in rates, including higher rates paid on deposits, a greater proportion of time and savings deposits relative to demand deposits, strong loan demand, and tight liquidity pressures on most rural banks.

Among district states, interest rates vary widely. The average rate reported on farm operating loans, for instance, ranged from a low of 10.25 percent in Illinois and Iowa to a high of nearly 11.75 percent in Michigan. Rates on operating loans averaged 10.5 percent at Wisconsin banks and nearly 11 percent at rural banks in Indiana.

Bank liquidity is a function of many variables. Several measures in the latest survey indicate that the liquidity pressures on district agricultural banks tightened further in the first quarter. For instance, the index of fund availability—which reflects a combination of deposit growth, the flexibilities and incentives that banks have for shifting funds between security and loan portfolios,

Selected measures of credit conditions at Seventh District agricultural banks

	Loan demand (index)[2]	Fund availability (index)[2]	Loan repayment rates (index)[2]	Average rate on feeder cattle loans[1] (percent)	Average loan-to-deposit ratio[1] (percent)	Banks with loan-to-deposit ratio above desired level[1] (percent of banks)
1975						
Jan-Mar	134	108	65	8.84	56.4	28
Apr-June	142	120	80	8.76	56.3	22
July-Sept	133	131	105	8.81	57.0	22
Oct-Dec	134	130	100	8.80	56.6	23
1976						
Jan-Mar	142	130	101	8.74	56.2	20
Apr-June	147	134	102	8.79	57.3	24
July-Sept	140	124	93	8.76	59.2	25
Oct-Dec	150	130	81	8.71	58.8	26
1977						
Jan-Mar	161	115	79	8.71	59.4	28
Apr-June	169	103	66	8.74	61.2	38
July-Sept	161	77	52	8.79	63.5	46
Oct-Dec	147	86	59	8.85	62.3	41
1978						
Jan-Mar	152	79	64	8.90	63.7	44
Apr-June	148	73	81	9.12	64.5	46
July-Sept	158	64	84	9.40	65.8	52
Oct-Dec	135	62	93	10.14	65.4	50
1979						
Jan-Mar	156	51	85	10.46	67.3	58

[1]At end of period.

[2]Bankers responded to each item by indicating whether conditions during the current quarter were higher, lower, or the same as in the year-earlier period. The index numbers are computed by subtracting the percent of bankers that responded "lower" from the percent that responded "higher" and adding 100.

and other factors—declined to 51 in the first quarter. That represents a substantial reduction from the very low levels last year.

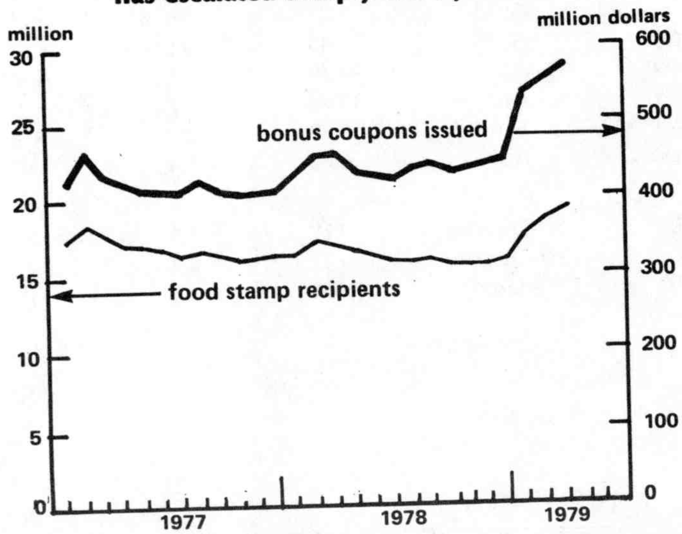
Further evidence of the tightening liquidity pressures was reflected in the unusually large first quarter increase in loan-to-deposit ratios. As of April 1, the ratio of loans to deposits at rural banks averaged 67.3 percent. That represents an increase of nearly 2 percentage points from three months earlier, an increase of 3.5 percentage points from a year earlier, and an increase of nearly 8 percentage points from two years earlier. Among district states, the average ratio ranges from a low of 64 percent at banks in Indiana to a high of 71 percent at rural banks in Wisconsin. In conjunction with the high ratios, nearly 60 percent of the bankers regard their current ratios to be above the desired level. A year ago, less than 45 percent of the bankers reported such a view and two years ago only 28 percent of the bankers felt their ratio exceeded the desired level.

The implications of these survey results are somewhat mixed. From the standpoint of recent and prospective strong farm earnings, the financial health of the overall farm sector does not appear to be a major concern. Nevertheless, some grain farmers are probably still having cash flow problems because of high input costs and comparatively small increases in grain prices. And the ability of rural banks to continue to meet the growing farm loan demand has been somewhat impaired by liquidity pressures. Banks have made a major contribution in meeting farmers' credit needs. But some banks may have to resort to new sources of funds if they are to retain their dominance in farm lending. And interest rates on farm loans will have to remain competitive if agriculture is to share proportionately with other sectors in the credit markets.

Gary L. Benjamin
Agricultural Economist

FOOD STAMP PROGRAM participation has risen sharply since year-end, primarily in response to the elimination of the coupon purchase requirement. Preliminary estimates indicate that roughly 19.1 million people received food stamp benefits in March, up sharply from 15.9 million in December but still below the record 19.3 million in May 1975. Under provisions of the Food and Agriculture Act of 1977, people qualifying for food stamps no longer have to buy part of their coupon allotments. This change, together with the many new procedures for determining eligibility, was expected to result in a net increase in the total number of recipients, but to redirect more of the benefits to people with lower incomes and, in so doing, eliminate some former recipients. Because of the surge in participation and the boost in benefits, however, there is some concern that the 1977 act's appropriations ceiling of $6.16 billion for fiscal 1979 will be reached before the September 30 year-end.

Participation in the food stamp program has escalated sharply since year-end



SOURCE: U.S. Department of Agriculture

The purpose of the food stamp program is to provide eligible households with the opportunity for nutritionally adequate diets. Two of the longstanding administrative problems with the program have been making sure that food stamps went only to eligible households and that all eligible households could participate if they so desired. To that end, a significant program change took effect January 1, when all states were required to begin implementing the elimination of the purchase requirement. It was estimated that elimination of the purchase requirement would add 3 million new participants.

In another effort to make food stamps more accessible to qualified people, a new and simplified application form has been devised. And unlike in the past, when some people could not participate because they could not get to the certification office due to disability or old age, interviews can now be conducted in their home or by mail or telephone. Requirements for bilingual caseworkers and material in some areas are expected to make program benefits available to more non-English speaking people. Increased cooperation between government agencies is expected to simplify the application and recertification processes for people qualifying for food stamps and other types of aid.

New procedures for determining program eligibility suggest that some people formerly receiving food stamps will no longer qualify because of the lower income limits. And more of the benefits will now go to people with lower incomes. Under the new program, an applicant's gross income includes his earned income as well as any other types of goverment financial aid he receives. By March 1, all states had to begin implementing these new rules for determining income eligibility and coupon allotments for all new applicants and for all recertifications of existing participants.

Income eligibility standards are derived from federal poverty guidelines set by the Office of Management and Budget and adjusted every July 1. Coupon allotments are adjusted every January 1 and July 1 to reflect changes in the Consumer Price Index for the six months ended the preceding September 30 and March 31. A family of four with a gross annual earned income of $10,225 or less currently qualifies for food stamp benefits. As of July 1, that threshold will rise to $11,340. A family of four with no net income—after subtracting allowable deductions—now receives $191 worth of coupons monthly. This will increase to $204 on July 1. The July increases in coupon allotments approximate 7 percent, although there is some variation by size of household because of the method of calculation.

The new program allows only three deductions from gross income. First, all households get a standard deduction that is adjusted every January and July to reflect cost-of-living changes. The standard deduction is currently $60, but on July 1 that will increase to $70. Second, households with employment income may deduct 20 percent of their total monthly earned income. Third, some households get a deduction of up to $80 for excess shelter costs and for actual day care costs that are necessary to enable a person in the household to work or seek employment. This deduction—adjusted annually—rises to $90 on July 1. Excess shelter costs are those that exceed half their gross income less all other allowable deductions.

Don A. Langford
Agricultural Economist

Selected agricultural economic developments

Subject	Unit	Latest period	Value	Percent change from Prior period	Percent change from Year ago
Index of prices received by farmers	1967=100	April	244	− 0.8	+17
Crops	1967=100	April	212	− 0.9	+ 2
Livestock	1967=100	April	272	− 0.7	+30
Index of prices paid by farmers	1967=100	April	245	+ 0.8	+13
Production items	1967=100	April	246	+ 1.2	+15
Producer price index* *(finished goods)*	1967=100	April	211	+ 1.1	+10
Foods	1967=100	April	228	+ 0.8	+11
Processed foods and feeds	1967=100	April	222	+ 0.9	+11
Agricultural chemicals	1967=100	April	209	+ 1.8	+ 9
Agricultural machinery and equipment	1967=100	April	225	+ 0.7	+ 8
Consumer price index** *(all items)*	1967=100	March	209	+ 1.0	+10
Food at home	1967=100	March	230	+ 0.8	+14
Cash prices received by farmers					
Corn	dol. per bu.	April	2.24	+ 0.9	0
Soybeans	dol. per bu.	April	7.00	− 2.1	+ 8
Wheat	dol. per bu.	April	2.98	+ 0.3	+ 6
Sorghum	dol. per cwt.	April	3.52	− 1.4	− 3
Oats	dol. per bu.	April	1.27	0	+ 7
Steers and heifers	dol. per cwt.	April	76.40	+ 3.5	+52
Hogs	dol. per cwt.	April	44.30	−10.3	− 2
Milk, all sold to plants	dol. per cwt.	April	11.60	− 1.7	+15
Broilers	cents per lb.	April	28.2	− 2.4	+ 1
Eggs	cents per doz.	April	60.2	− 6.4	+16
Income *(seasonally adjusted annual rate)*					
Cash receipts from farm marketings	bil. dol.	1st Quarter	125	+ 6.5	+20
Net realized farm income	bil. dol.	1st Quarter	33	+ 5.4	+29
Nonagricultural personal income	bil. dol.	March	1,804	+ 1.1	+12

*Formerly called wholesale price index.

**For all urban consumers.

FEDERAL RESERVE BANK OF CHICAGO
Public Information Center
P. O. Box 834
Chicago, Illinois 60690
Tel. no. (312) 322-5112

FEDERAL RESERVE BANK OF CHICAGO
AGRICULTURAL LETTER

FIRST-CLASS MAIL
U.S. POSTAGE
PAID
Chicago, Il.
Permit No. 1942

US3442D MR. O.B. JESNESS
INSTITUTE OF MINN.
UNIVERSITY OF MINN.
ST. PAUL, MN 55108