FEDERAL RESERVE BANK OF CHICAGO

AGRICULTURAL LETTER

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prices

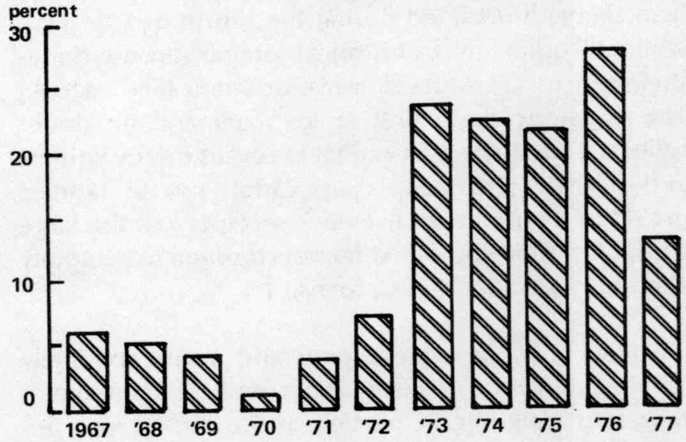
THE LAND VALUE AND CREDIT CONDITIONS survey recently completed indicated a slight increase in Seventh District farmland values during the fourth quarter, while agricultural credit conditions seemed marginally improved. Survey responses of approximately 600 District agricultural bankers revealed a 2 percent rise in the value of good farmland during the October-December period. Coinciding with the recovery in the farmland market, it appears the deteriorating agricultural credit conditions noted during the summer months were arrested during the fourth quarter. In a historical perspective, District agricultural banks experienced exceptionally tight liquidity pressures during the fourth quarter; however, relative to the previous quarter, it appears that the pressures have stabilized and perhaps even eased somewhat.

The fourth-quarter recovery in grain prices in conjunction with improved earnings of livestock producers and the record movement of corn under loan are presumably major contributors behind the improvements noted in the most recent quarterly survey. Cash corn prices at Chicago averaged $2.20 per bushel during December—an increase of approximately 20 percent from the September average of $1.85 per bushel. Similarly, wheat prices, averaging $2.65 per bushel during December, rose 20 percent during the period. Although a less spectacular increase, the 13 percent rise in the price of soybeans during the fourth quarter was no less meaningful in light of the record 1977 harvest. During this same period, Omaha hog and cattle prices rose nearly 7 and 5 percent, respectively, enhancing further livestock producers' gross receipts.

prices

Illinois farmland values, which declined substantially in the third quarter, rose 4 percent during the fourth quarter pacing the quarterly upturn among District states. Agricultural bankers in District portions of Wisconsin reported a 3 percent increase for the period, while bankers in both Michigan and Indiana indicated 2 percent rises. Iowa bankers reported no change for the second consecutive quarter. Although year-to-year increases in land values (prices) were recorded among all District states, the overall average of 13 percent was the lowest in five years. Bankers in Illinois reported the smallest annual rise (7 percent), while those in Wisconsin reported the largest (21 percent).

Smallest annual gain in five years for District farmland values



For the second consecutive quarter—and only the second time since 1970—the proportion of bankers anticipating lower-trending farmland values in the current quarter exceeded the proportion expecting an increase. Among individual District states bankers' responses varied somewhat regarding anticipated first-quarter trends in farmland values. The proportion of the District's agricultural bankers in both Wisconsin and Michigan who expected upward pressures on land prices in the current quarter substantially exceeded the proportion expecting a downturn, while the converse was true with bankers from Illinois, Indiana, and Iowa. In all District states, however, the vast majority of the bankers anticipated land values would be stable during the current quarter.

prices

The fourth-quarter upturn in farmland values adds to concerns about farmers' cash flows. Grain prices during the period averaged well above the 1977 lows registered during the preceding quarter. Farmers were completing harvests of record or near-record proportions in many areas and the announced shortfall in the

Russian harvest provided an impetus in boosting grain prices at a faster rate than the 1977 farm bill could have effected alone. Consequently, land rental rates probably failed to show reductions of the magnitude expected by many observers. In the absence of any weather-related pressures, the recent buildup in grain stocks suggests grain prices may well hover near loan levels. Consequently, corn and soybean prices for the next few months will likely continue to average well below the first-half 1977 levels of $2.30 and $8.00 per bushel, respectively. The outcome may be squeezed margins for many farmers which, in turn, may preclude significant upward pressures on famland prices.

Agricultural credit conditions at Seventh District rural banks reflect a strong farm loan demand, a slight improvement in fund availability, stable interest rates, and continuing concerns about debt repayment capabilities of some borrowers. The index of agricultural loan demand declined during the fourth quarter and, while still quite high by historical comparison, was nonetheless at its lowest level in five quarters. [See page 4.] The apparent slackening in loan demand no doubt reflects a curtailment in capital expenditures by farmers and perhaps the stepped-up cash flows to farmers provided by increased livestock receipts and the large amount of funds provided farmers through Commodity Credit Corporation (CCC) loans.

Slow loan repayment rates and an exceptionally high incidence of renewals and extensions continue to represent a significant portion of the overall loan demand. Over 55 percent of the responding bankers indicated an increased level of renewals and extensions relative to a year earlier, while half reported a slower rate of loan repayment. With the exception of the third quarter, these measures remain at abnormally high levels. Among District states slow loan repayments and increased renewals and extensions appear most widespread in Illinois, Indiana, and Iowa—the District's major grain-producing area.

Loan-to-deposit ratios declined nominally in each of the District states during the fourth quarter. The ratios reported as of January 1 averaged 62.3 percent; down a little over 1 percentage point from the record of the preceding quarter, but well above the relatively high year-earlier level of 58.8 percent. The average ratio among banks in District portions of Illinois rose nearly 5 percentage points last year, while Wisconsin, Iowa, and Indiana banks reported increases of 4, 3, and 3 percentage points, respectively. Michigan agricultural banks, which showed no change from a year ago, nevertheless had the second highest average ratio among the five states. These unusually large year-to-year increases—in light of other evidence of fairly substantial growth in deposits at agricultural banks—indicate District agricultural bankers are accommodating the strong demand for farm loans.

Interest rates charged on farm loans during the October-December period remained essentially stable for the twelfth consecutive quarter. Rates charged for feeder cattle loans averaged 8.85 percent, while those for farm operating loans and farm mortgages averaged 8.91 and 9 percent, respectively. Agricultural banks in District portions of Wisconsin, Michigan, and Indiana continue to charge higher interest rates for all types of farm loans than their counterparts in Iowa and Illinois.

A slight majority of the respondents anticipate year-to-year increases in the volume of non-real estate farm loans during the January-March period. Among the various categories of non-real estate farm loans, the largest increases during the current quarter are expected to occur in the demand for operating credit. Demand for farm machinery loans on the other hand is expected to lag the year-ago pace, according to 45 percent of the respondents. This is an unusually large proportion exceeded only by the preceding quarter's survey results.

Over the next three- to six-month period, roughly three-fifths of the responding agricultural bankers anticipate an increase from recent experience in the need to refinance short-term farm debt with long-term commitments. Approximately 55 percent of the respondents expect increased requests for renewals and extensions, while 43 percent expect lower farm loan repayment rates. Roughly 15 percent of the bankers anticipate a higher rate of default on farm loans during the period, although nearly four-fifths of the respondents expect no change from recent past experience. Approximately two-fifths of the reporting bankers anticipate higher deposit growth at their banks during the first half of 1978.

Roughly one-half of the bankers expect the overall farm credit situation to tighten further during the next three to six months, while only 4 percent expect the situation to ease. In appraising the outlook for their banks' liquidity positions during this period, nearly one-third of the respondents anticipate a further deterioration, while an easing is expected by another 11 percent.

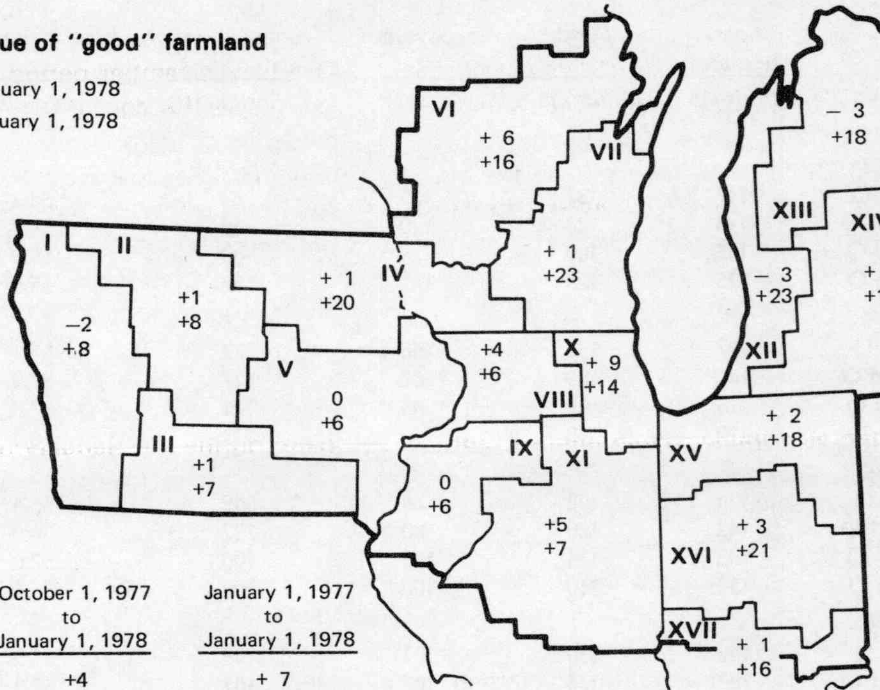
In an overview of the latest quarterly survey's findings, it appears that fourth-quarter agricultural credit conditions may have improved marginally over the third-quarter status. Nevertheless, bankers' views for the first half of 1978 indicate that problems are still widespread and warrant careful monitoring by both lenders and farmers.

Don A. Langford
Agricultural Economist

Trends in District farmland values

Percent change in dollar value of "good" farmland

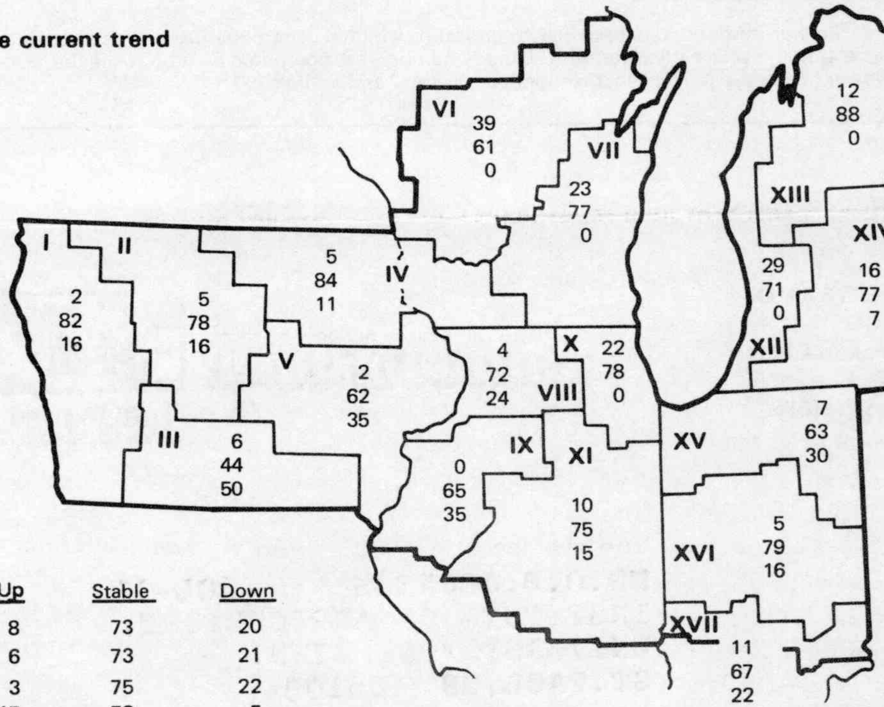
Top: October 1, 1977 to January 1, 1978
Bottom: January 1, 1977 to January 1, 1978



	October 1, 1977 to January 1, 1978	January 1, 1977 to January 1, 1978
Illinois	+4	+ 7
Indiana	+2	+19
Iowa	0	+ 9
Michigan	+2	+15
Wisconsin	+3	+21
Seventh District	+2	+13

Percent of banks reporting the current trend in farmland values is;

Top: Up
Center: Stable
Bottom: Down



	Up	Stable	Down
Illinois	8	73	20
Indiana	6	73	21
Iowa	3	75	22
Michigan	17	78	5
Wisconsin	27	71	2
Seventh District	10	74	16

Trends in credit measures among District agricultural banks

	Loan demand (index)*	Fund availability (index)*	Loan repayment rates (index)*	Loan renewals and extensions (index)*	Average loan-to-deposit ratio (percent)	Banks with loan-to-deposit ratio above desired level (percent of banks)
1973						
1st Q	147	137	125	84	54.2	17
2nd Q	144	123	120	89	56.4	21
3rd Q	135	100	124	80	56.3	22
4th Q	125	125	142	67	55.5	20
1974						
1st Q	127	133	136	72	54.1	17
2nd Q	142	89	87	117	57.9	27
3rd Q	126	69	85	121	57.3	32
4th Q	122	98	79	127	56.9	32
1975						
1st Q	134	108	65	145	56.4	28
2nd Q	142	120	80	122	56.3	22
3rd Q	133	131	105	100	57.0	22
4th Q	134	130	100	103	56.6	23
1976						
1st Q	142	130	101	109	56.2	20
2nd Q	147	134	102	102	57.3	24
3rd Q	140	124	93	109	59.2	25
4th Q	150	130	81	124	58.8	26
1977						
1st Q	161	115	79	125	59.4	28
2nd Q	169	103	66	140	61.2	38
3rd Q	161	77	52	152	63.5	46
4th Q	147	86	59	151	62.3	41

*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.

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