

an economic review by the Federal Reserve Bank of Chicago

Business Conditions

**The economy,
the Midwest, and Chicago**

**District farmland
values soar**

Banking developments

***april
1974***

Contents

The economy, the Midwest, and Chicago 3

Economic trends in the six-county Chicago area seldom vary from national patterns because of the area's great size, central location, and its extensive diversity of industry.

District farmland values soar 8

Farmland values in the Midwest experienced the sharpest annual increase in a half century in 1973. Considering projected levels for farm income and mortgage rates, land values are likely to continue an upward trend in 1974.

Banking developments 13

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The economy, the Midwest, and Chicago

The preliminary estimate of the Department of Commerce indicates that "real GNP"—the dollar value of the nation's total output of goods and services adjusted for price changes—declined in first-quarter 1974 at a seasonally adjusted annual rate of almost 6 percent—the sharpest drop since the first quarter of 1958. The "GNP deflator," a measure of changes in the general price level, rose at an annual rate of almost 11 percent in the first quarter, the worst performance since 1951, during the Korean War.

These disturbing statistics are not unexpected news. They reflect first, the adverse impact of the petroleum shortage, principally on the output of the auto, petroleum refining, airline, and recreation-related industries; and, second, the depressed housing market where the adverse effect of high market interest rates was compounded by uncertainties related to fuel supplies. The accelerated rate of price inflation in the past several months has been apparent to consumers because it has been centered in food, gasoline, and other fuels.

It is hoped that the drop in total real output has leveled off and that the second half of 1974 will see some revival of growth that will continue into 1975. Virtually without exception, capital goods producers, who are particularly important in the Midwest, are experiencing unprecedented strength in demand. The capital goods boom did not falter during the embargo, and, on balance, probably was

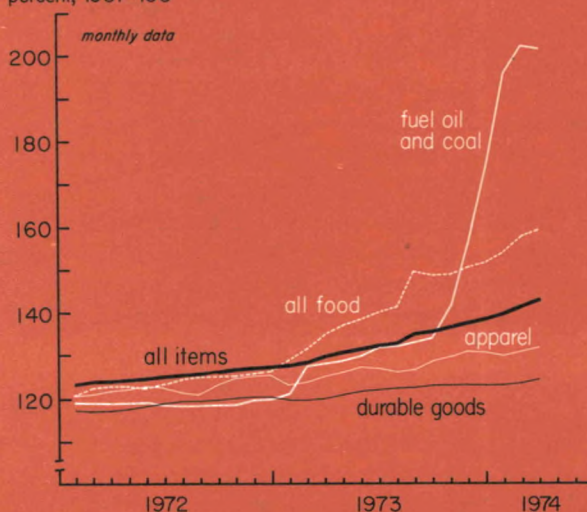
strengthened. Moreover, markets for most types of consumer goods and services did not soften during this troubled period, and those sectors that were most seriously affected—full-sized cars and recreational vehicles—have shown improvement recently.

The housing industry has shown a few signs of revival, but the recent upsurge in interest rates has raised the spectre of renewed "disintermediation," deteriorating inflows of savings to the thrift institutions that provide the bulk of funds for residential mortgages. The tight money situation in residential mortgages is pronounced in Illinois, mainly because of the 8 percent usury rate which is currently below rates prevailing in other states.

The generally accepted definition of a

Food and fuel have led the rise in consumer prices

percent, 1967=100



"recession" is two consecutive quarterly declines in real GNP. It is possible that the terms of this definition will not be fulfilled in 1974. But even if this were to be the case, the economic consequences of the Arab-Israeli war cannot be equated with a classical recession in which most sectors of the economy display weakness. Undoubtedly, there was a possibility that a cumulative decline might have spread throughout the economy in late 1973 and early 1974. But the danger appears to have lessened.

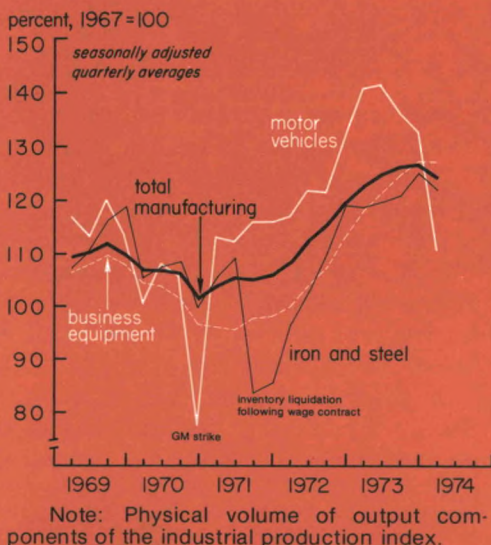
Despite widespread expressions of pessimism, the bulk of consumers, businessmen, and lenders have maintained their morale and have not retrenched their spending plans. The economic intelligence efforts of the Federal Reserve System continue to remain alert to the many pitfalls inherent in the unstable environment of the past six months as they monitor and appraise economic developments at home and abroad.

Chicago and the Seventh District

Overall economic trends in the Chicago area—six counties in Illinois and two in northern Indiana—seldom vary significantly from the national pattern. This is because of the area's great size, its central location, the extensive diversification of its manufacturing and service industries, and its position as the Midwest's economic metropolis of industry, agriculture, trade, and finance.

The Chicago area's population now exceeds 7.8 million people, placing it third behind New York and Los Angeles (broadly defined). Over 5.5 million people live in Cook County, of whom 3.4 million are in the central city. In the decade of the Seventies, the population of the eight-county Chicago area increased by 12 percent, compared to 13 percent for the United States as a whole. The population of the city of Chicago declined 5 percent from 1960 to

Strength in capital goods contrasts with slump in autos



1970. (The boundaries of the city have been circumscribed for many years.) In part, this was the result of demolitions of residential structures resulting from urban renewal and the building of expressways. Declines in the population of core cities have been common throughout the nation. But population growth in the remainder of Cook County, and in the seven outlying counties, continued at a fairly rapid pace. With declining birth rates in recent years, population growth has slowed in the entire Chicago area, probably about as much as in the nation.

When the Federal Reserve System was organized in 1914, Chicago was an obvious choice for the location of one of the regional Federal Reserve banks. The Seventh Federal Reserve District as delineated in 1914 included, and still includes, all of Iowa and the major portions of Illinois, Indiana, Michigan, and Wisconsin. These states, which have 16 percent of the nation's population, produce 22 percent of its manufactured products and about the

same proportion of its agricultural products. On the other hand, it has a smaller than proportional share of the nation's extractive industries, lumbering, recreational activities, and government.

The Corn Belt, which contains the richest farmland in the nation (if not in the world), cuts a wide swath through Iowa, Illinois, and Indiana. The district produces about one-half of the nation's corn and soybeans, and markets about one-half of its hogs. In manufacturing, motor vehicle output remains concentrated in Michigan, which has over 40 percent of the industry. The five-state region, taken as a whole, has a substantial stake in the currently booming capital goods industries. These states produce over 30 percent of the nation's steel and at least 30 percent of its producer goods. For farm, construction, and metal-working equipment the share is much larger. In consumer goods, the five states produce 50 percent of the nation's television sets, and over 30 percent of its household appliances. The region, therefore, is relatively strong in "hard" as opposed to "soft" goods.

Chicago's contribution

The Chicago area is the natural focal point of the industry and trade of the Midwest. It provides transportation, financial, warehouse, and other services for surrounding states and areas.

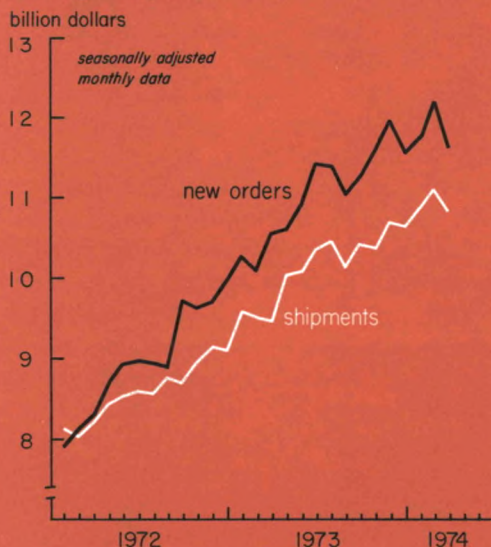
The growth and continued vitality of the Chicago area are due largely to its location. Few places in North America were so clearly foreordained as great centers of population, industry, commerce, and finance as the land surrounding the mouth of the Chicago River and extending south along the foot of Lake Michigan. The area is unique in that it stands astride the waterways of the Great Lakes and the Mississippi and its tributaries. Moreover, Chicago is the natural center of the air, rail, and road transportation systems con-

necting the Midwest with other regions of the nation.

Aside from transportation, the Chicago area benefits from the flat terrain extending far into the hinterland. Real estate developments can proceed with a minimum of costly site preparation. In common with other Great Lakes cities, the Chicago area has ample fresh water for industrial and domestic purposes. These and other advantages—a large and varied labor force, availability of business services, ample capabilities of local utilities, and educational and cultural facilities—maintain the area's economic vigor.

In addition to the Federal Reserve Bank, Chicago is the home of the Board of Trade, the Mercantile Exchange, the Midwest Stock Exchange, and the region's Home Loan Bank. These organizations, along with the commercial banks and other financial institutions located in Chicago, are playing ever-larger roles in the national and international economic structure. In the past year, a number of the

New orders for business equipment continue to outpace rising shipments



largest foreign banks have applied for the right to establish branches in Chicago.

Diversified employment

About 3 million people currently are employed in nonfarm wage and salary jobs in the Chicago area, of whom 30 percent are in the relatively volatile manufacturing sector. For the nation as a whole, manufacturing accounts for 26 percent of total payroll employment. In Milwaukee and Detroit, 35 percent of the jobs are in manufacturing, and in many smaller centers the proportion substantially exceeds 40 percent. Within manufacturing, the Chicago area's most important single industry is steel, with mills located in the South Chicago-northern Indiana area. For many years, this has been the nation's leading steel center. New steel plants have been added in the past decade and additional expansion plans are underway. Despite the recent sharp decline in shipments to the auto industry, the steel mills continue to operate at effective capacity.

About 30 percent of the Chicago area's manufacturing employment is in either the "electrical machinery" or "nonelectrical machinery" classifications. But these are statistical groupings rather than industries. Firms so-classified produce a wide variety of components and finished equipment for industry, agriculture, construction, mining, utilities, and transportation, as well as appliances, TV sets, lighting, and recreational equipment for consumers. The area also produces a wide variety of "nondurables"—petroleum products, processed foods, and apparel. Demand for virtually all these products continues to be very strong.

Perhaps more than any other center, the Chicago area represents a scaled-down version of the nation as a whole. By and large, therefore, economic developments in the Chicago area parallel national trends.

Consumers spend freely on most goods as autos sag



In recent years, however, growth in employment in the Chicago area, as in most other large metropolitan areas, has lagged the national performance. This reflects, in part, the national trend toward decentralization of industry to smaller, nonmetropolitan (even rural) areas. But, in the case of Chicago, it may also reflect the lack of sufficient numbers of qualified workers. The unemployment rate estimated for the Chicago area as a whole in February 1974 was 3.6 percent, compared with 5.2 percent for the nation.

For many years, the unemployment rate estimated for the Chicago area has been well below the national rate, and also below the rate for most of the very large metropolitan areas. Because of its diversification, the Chicago area was not significantly affected either by the defense cutbacks that followed 1968, or the sharp slump in sales of passenger cars that began last fall. On the other hand, it has not had the same degree of stimulus from the capital goods boom that has been so noticeable in Milwaukee, Peoria, Rockford,

and the Quad Cities areas.

Although the unemployment rate for Chicago has remained relatively low, the situation varies sharply among the hundreds of municipalities included in the eight-county metropolitan area and within the city of Chicago itself. In the core city there are neighborhoods, mainly with minority group populations, that have very high rates of unemployment. In addition, these depressed sectors of the city have many people of working age who are not counted as part of the labor force—neither employed nor seeking work because of a variety of reasons.

While some sections of the city have unemployment problems, in other parts of the city, and in many of the suburbs, employers have complained of shortages of trained or trainable workers in the past year or so. This repeats the experience of the middle and late 1960s. The city has witnessed a long-term exodus of industry to the suburbs or to smaller centers outside the metropolitan area. Throughout the Chicago area, the problem of matching people and jobs is intensified by two formidable obstacles: (1) inadequate educational attainment of job seekers, and (2) lack of suitable transportation.

Looking ahead

The experience of the nation's economy since World War II has not been kind to chronic pessimists. Recessions have been short and shallow, by the standards of earlier history, and many widely heralded recessions have not, in fact, materialized. If such predictions for 1974 prove wrong for the nation they will certainly be wrong for the Chicago area, which is not vulnerable to upsets in a few specific industries.

The uptrend in capital expenditures by business appears to have great momentum. New orders continue to outrun rising

shipments, and order backlogs, in many cases, stretch into 1975 and beyond. Increases in output in many firms are hampered by serious shortages of plant capacity, materials, components, and skilled labor. In the energy field, even assuming a continued flow of Mideast oil, enormous investments in new facilities are expected to be required for many years to come.

Consumers, despite their pessimistic responses to consumer surveys, continue to spend fairly freely. Through mid-April, consumer outlays on goods, other than autos, were up 10 percent from last year, a somewhat larger increase than for after-tax income. With improved supplies of gasoline, sales of full-sized cars and recreational vehicles can be expected to improve—indeed, there are signs that this has already begun. Consumer incomes will be boosted in 1974 and following years by large increases in worker compensation, pensions, and other payments. Increasingly, income recipients are “protected” against inflation by escalation agreements tied to the consumer price index.

The extremely rapid price inflation of the recent period is likely to moderate somewhat as food and fuel supplies improve in the months ahead. But it would be unwise to count on a drastic slowing in the rate of rise in the general price level. Prices of many manufactured goods, and of many services, have not yet “caught up.” The gradual disestablishment of price controls will certainly encourage producers to pass on higher costs as they are incurred.

Midwest consumers and businesses purchase goods and services in markets that, for the most part are strongly influenced by national trends. For example, changes in the consumer price index for the Chicago area parallel the national index fairly closely. Control of inflation is not a local or regional matter but requires the full endeavor of the nation.

District farmland values soar

Farmland values in the Midwest rose nearly one-fourth last year. Although the value of farmland in the Seventh District has exhibited a persistent upward trend since 1940, the 1973 rise was the sharpest annual increase in over a half century.

Increases in the value of district farmland were pervasive, although the rate of increase varied widely from state to state. Farmland values in Illinois and Iowa recorded the largest gains, up 28 percent and 26 percent, respectively, from a year earlier. Indiana land values increased 24 percent, Michigan farmland prices increased 19 percent, and those in Wisconsin rose 16 percent.

Farmland values are determined by the interaction of numerous demand and supply forces. While the reasons for changes in farmland values are often obscured and difficult to isolate, at least four factors combined in 1973 to provide the impetus for the largest increase in modern times.

- The improvement in current and prospective crop prices significantly increased the net returns on farmland.
- Credit to finance the purchase of farmland was readily available.
- Pressures to enlarge the size of farm operations were increased as farmers upgraded machinery inventories.
- Farmland prices have increased faster than the rate of inflation causing many investors to consider farmland as a hedge against inflation.

Farm incomes and land prices

Record crop and livestock prices resulted in a sharp rise in farm incomes in 1973. Agricultural prices, reflecting surging domestic and international demand,

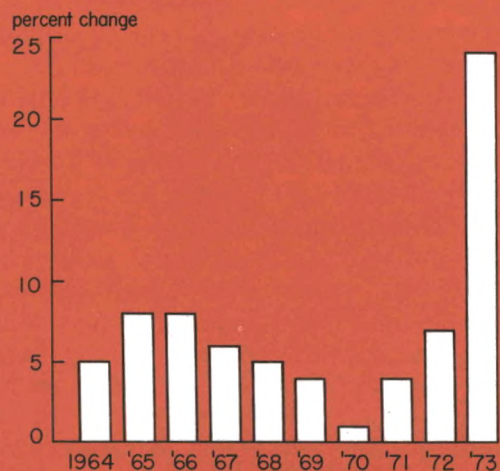
were up about one-third, and net U.S. farm income reached an unprecedented \$26 billion, over 30 percent higher than a year earlier and nearly 60 percent larger than the average for the previous five years.

Most Seventh District farmers experienced even larger income gains than did farmers in the nation as a whole. Total cash receipts from farm marketings at the national level were up 38 percent, but Indiana farmers experienced a 57 percent increase, Illinois farmers a 49 percent increase, and Iowa farmers a 44 percent increase. All three of these states are heavily engaged in grain production, the strongest sector of agriculture during 1973. Cash receipts from farm marketings in Michigan and Wisconsin rose less than in other district states, reflecting the more diverse range of commodities grown in those states.

Higher income levels placed farmers in a very liquid financial position and they were able to allocate large sums from their cash flow to purchase real estate which, in effect, increased demand. At the same time, the higher income levels provided greater incentives for those who presently own farmland to retain ownership and thereby reduce the available supply of transferable land. Both situations served to apply upward pressures on land prices.

A major influence on the value of farmland is the sum of expected future returns discounted to the present. The impact of changes in current and expected income on the price of farmland can be illustrated by the change in per acre returns of a typical corn farm. Over the past several years, net returns averaged around \$25 per acre. However, during 1973 returns jumped to about \$100 per acre. If the different income levels were capitalized

District farmland values recorded astounding increases . . .



into land values utilizing an 8 percent interest rate, which assumes that the income levels continue indefinitely, the value would have increased from approximately \$300 per acre to nearly \$1,300 per acre.

More than one year's earnings must be considered, of course, when evaluating the income-producing ability of farmland. While it's unlikely that farm income will remain at the 1973 level indefinitely, returns on farmland are expected to be higher in the near future than in the years just prior to 1973.

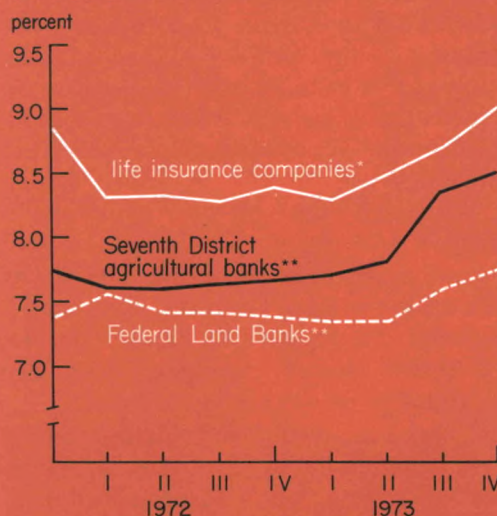
Farm real estate credit

Ample availability of credit facilitated the rapid expansion in farm real estate land values in 1973. Both the total amount of farm real estate credit extended and the year-to-year increase rose to record levels. Paralleling the increase in credit extensions, the proportion of farmland transfers involving credit and the proportion of the purchase price financed by credit rose to record highs. The ratio of debt to purchase

price reached 78 percent in 1973, 4 percentage points more than the previous high. Similarly, the percentage of farm real estate transfers on which debt was incurred stood at 86 percent throughout 1973, 4 percentage points more than the previous year and a new record.

Interest rates charged by institutions for farm mortgage funds held relatively steady in the first half of 1973 but then turned sharply upward in the second half. By year-end, the average interest rate on farm real estate loans charged by major real estate lenders ranged from 7.75 to 9 percent, from nearly .50 to .75 of a percentage point over the rate of a year earlier. Nevertheless, those willing to pay the higher interest costs apparently had little problem obtaining farm real estate credit in the second half as reflected by the rapid increase in new real estate loans provided by the institutional lenders.

. . . despite rising farm mortgage interest rates in 1973



*Average rate on new commitments made during quarter.

**Average rate at end of quarter.

Both income and interest rate changes affect farmland values

Interest rates	Net income per acre				
	\$20	\$40	\$60	\$80	\$100
	<i>(dollar value)</i>				
5	400	800	1,200	1,600	2,000
6	333	667	1,000	1,600	2,000
7	286	571	857	1,143	1,429
8	250	500	750	1,000	1,250
9	222	444	667	889	1,111
10	200	400	600	800	1,000

Rising interest rates, and credit conditions that have generally prevailed during such periods, usually affect farmland values in a negative manner. The most recent example was the 1969-70 credit crunch when growth in Seventh District farmland values halted, and in many instances actually declined. High interest rates reduce the amount of credit a farmer can service for a given amount of income and, therefore, the amount of land he can purchase on credit. Moreover, increasing interest rates discourage many farmers from refinancing mortgages obtained at lower rates in earlier years. Also, tight credit conditions usually signal increases in downpayments, shorter maturities, and an overall reduction in available farm real estate credit—all depressing factors on the land market.

Although the effects of changing credit conditions are impossible to measure accurately, the impact of interest rates on land values can be illustrated by discounting the expected income per acre by different interest rate levels. For example, at a 7 percent interest rate, land that produces an annual net income of \$40 would be valued at \$571 per acre. If interest rates rise to 8 percent, the same land would be valued at \$500 per acre, all other things equal. Therefore, rising interest rates usually act as a deterrent to increases in farmland values.

The increase in actual and expected income, however, more than offset the increase in interest rates during 1973. Moreover, other conditions generally associated with tight credit—increased downpayment requirements and shorter repayment schedules—failed to materialize.

Federal Land Banks (FLBs) led all other institutional lenders in extensions of farm real estate loans during 1973. New money loaned by FLBs in Seventh District states was up 50 percent from the previous year and outstandings stood 10 percent above the year-earlier level. At the national level, the volume of new FLB loans also grew 50 percent, but outstandings grew almost twice as fast as in the Seventh District. The difference in growth of outstandings indicates paydowns at a much faster rate than at the national level, a reflection of the higher-than-average farm incomes in district states.

Relatively new, lower downpayment requirements on FLB loans may be contributing to rapid expansion in credit extended by FLBs. The Farm Credit Act of 1971 gave FLBs the authority to expand their loan limits from 65 percent of normal agricultural value to 85 percent of current market value. The effect of this change has been to reduce by more than 50 percent the legally required downpayment on land purchases financed by FLBs. A farmer with a given amount of investment capital, therefore, can bid more for the farmland and still finance the loan under the revised downpayment provisions.

Banks and insurance companies, the other major institutional lenders, also achieved notable increases in farm real estate credit volume. At year-end 1973, outstandings at Seventh District member banks were 12 percent higher than a year earlier. National data indicate that insurance company farm real estate mortgage volume was up 6 percent in 1973.

In contrast to the rapid expansion in credit extended by institutional lenders,

seller financing of farm real estate showed only modest increases during 1973. Sellers often prefer to transfer farmland via an installment sales contract because it allows the seller to spread capital gains tax payments over the life of the contract. According to the Internal Revenue Code, if less than 30 percent of the sale price of land is received in the year of the sale, capital gains tax will be due only as payments are received rather than on the full purchase price in the year of the sale. In addition, since interest payments must be reported as ordinary income, sellers of farmland will often decrease the interest rate charged on the transaction and inflate the price of the land.

Historically, seller financing has been the most important single source of farm real estate credit, and the trend has been for this source to expand in periods of tight credit and contract when the money market loosens. Such was the case in the tight credit period of 1969-70 when sellers financed approximately 60 percent of all farmland transfers. Last year, however, due mainly to the dramatic rise in farm real estate loan volume (up nearly $2\frac{1}{2}$ times over 1972), sellers financed only about 40 percent of the total.

Farm enlargement

Rising farm income levels in 1972 and 1973 allowed farmers to begin replacing farm equipment at a rapid pace. For instance, in 1972 tractor sales jumped 19 percent above the previous year, and aggregate sales of seven major farm machines rose 4 percent. As income rose further in 1973, farmers were encouraged to purchase additional equipment in order to utilize the accelerated depreciation schedules and the 7 percent investment tax credit that reduced taxable incomes and tax payments. Tractor sales increased 26 percent last year, and aggregate sales of the seven major farm machines jumped 22 percent.

As farmers acquire these large, expensive, high-capacity machines, many are motivated to add land to the existing enterprise in order to spread fixed cost over a larger base. Time constraints dictate that additional land be in rather close proximity to the existing farm, thereby limiting the potential supply of land for any individual farmer to a narrow geographic area. The limited source of supply suggests that higher prices for available land will be the normal result. And while the potential economies of scale may justify the higher prices for farmers who wish to enlarge their operations, such actions tend to raise the price of land for all buyers.

A hedge against inflation

Farmland values increased four times faster than the inflation rate during 1973, leaving owners well protected against the effects of the depreciating dollar. Inflation in business and industry as measured by the implicit price deflator for private GNP has averaged 3 percent compounded annually in the 25-year period 1947-72. The average price of an acre of farmland increased at nearly a 6.25 percent rate during the same time period. Consequently, a long-term investment in farmland has served as an effective hedge against inflation. Such prospects for future long-term capital gains have created speculative demand for farmland based solely on expectations of continued price increases.

The speculative trend is reflected by the number of farmland purchases made by nonfarmers from outside the area in which the farmland is located. According to Seventh District bankers, the proportion of nonfarmer buyers increased from 1970 to 1973 in each of the district states except Wisconsin.

Nonagriculture uses

An increasing amount of farmland

has been diverted to nonagricultural uses in recent years. In Seventh District states, the highest levels of diversion have occurred in Michigan and Wisconsin. It is estimated that 7 percent of the farmland sold in these Lake States during the year ending March 1, 1973 will probably be converted to recreational or residential use within five years. A rising level of affluence, shorter workweeks, and longer vacations have increased the demand for recreational properties and "second homes." In contrast, it is estimated that only 3 percent of the farmland sold in the Corn Belt States—which include Illinois, Indiana, and Iowa—is likely to be converted to such uses within five years.

As a result of the higher level of nonagricultural demand, the value of Michigan and Wisconsin farmland increased faster than in other district states throughout most of the 1960s and the early 1970s. While the demand for farmland for nonagricultural use in these states continued during 1973, it lost much of its urgency. Higher interest and the threat of fuel shortages are two major reasons why the demand abated. Wisconsin farmland prices increased only two-thirds as fast as the average of all district states in 1973, and Michigan farmland prices grew at about four-fifths the average for the district.

Outlook

The levels of farm income and interest rates will likely continue to be the most important factors influencing the demand for farmland in the months ahead. Net farm income is expected to range between \$21

and \$24 billion this year, down somewhat from 1973 due mainly to increases in the costs of production. Nevertheless, the projected level would be the second highest on record and undoubtedly will support further increases in land values, albeit at a slower rate than during 1973. Rising interest costs on new farm mortgage loans may further temper the advance in land prices. At the start of 1974, mortgage rates were from .50 to 1 percentage point higher than a year ago, and have moved generally upward since then.

Shortages of some key farm inputs, such as fuel and fertilizer, as well as restrictions on auto travel, also are likely to be negative factors affecting land prices, while the spillover effect of 1973's booming farm equipment sales could increase pressures for farm enlargements. A continuing high rate of inflation should serve to provide further support.

Through the first quarter of 1974, farmland values in the Midwest continued to rise at an accelerated rate. However, an increasing proportion of bankers foresee a stabilization of land prices in the months ahead. Such views would be consistent with changes in farmland values in similar previous periods. Historically, very rapid increases in farmland values have been associated with short-lived peaks in crop prices. Subsequent declines in crop prices have been followed by at least one year of decrease in land prices along with a cost-price squeeze on farmers, especially the most recent buyers of farmland.

Terry Francl

Banking developments

Consumer credit at banks

Instalment loans at the nation's commercial banks rose 16 percent in 1973—the same as total consumer instalment debt—thus maintaining their existing share of the instalment loan market. Banks accounted for 47 percent of total instalment credit outstandings at the close of 1973, against 25 percent for finance companies.

Mobile home loans were the fastest growing component of banks' instalment credit last year, rising 25 percent. Auto loans, which make up 45 percent of all commercial bank instalment credit, rose 15 percent. Banks reported relatively slower gains in home improvement loans last year than for other major types of instalment credit. Nonetheless, growth in home improvement loans outstanding was more rapid than in 1972 or 1971.

These national trends are reflected in the latest available instalment credit data for Seventh District banks (through mid-1973). In the 12 months ended last June 30, instalment loans at district banks rose 18 percent, nearly the same as the gain for all insured commercial banks in the nation. The increase was even larger in 18 of the Seventh District's 35 SMSAs—as high as 42 percent in Fort Wayne.

Auto loans, which increased 17 percent in the district, continued to account for the largest dollar increase, with outstandings comprising almost half of total consumer instalment debt at banks in the district SMSAs. Gains in bank card credit were even larger than the nationwide gain, and evidenced the growing importance of this activity in many areas. Credit card and check credit outstanding at district banks at mid-1973 was a little over \$800 million, nearly 28 percent higher than the

previous year's level. This category accounted for 8 percent of total instalment credit at district banks, about the same as a year earlier. Financing of other consumer durables, home improvement loans, and personal loans, on the other hand, rose less rapidly than nationally.

Mobile home loans

Although the purchase and financing of mobile homes have declined significantly in recent months, this marks a setback in a strong upward trend. Mobile home loans in the district were up 39 percent in the 12-month period ending last June 30, compared with a 34 percent increase for the nation. District outstandings were over \$1 billion in mid-1973. These loans accounted for nearly 11 percent of district banks' instalment credit, compared with 8 percent just two years earlier. At the national level, banks' portfolios of mobile home loans tripled in the period 1969-72. It is believed that commercial banks hold more than one-half of all mobile home credit, and these holdings comprise about 10 percent of all outstanding instalment credit at banks. To some degree, this rapid growth reflects the public's substitution of mobile homes for conventional housing.

Indianapolis banks are the district's biggest mobile home lenders with almost \$131 million outstanding, about 23 percent of all their consumer instalment loans.

Indiana and Michigan are among the leaders in mobile home manufacturing. Indiana district banks reported an increase of almost 68 percent in mobile home loans, with total outstandings of \$308 million at midyear 1973. Michigan banks, with \$289 million outstanding, slipped to second place in the district. A number of banks in

Consumer instalment loans at all insured commercial banks

	Outstanding, June 30, 1973 (millions of dollars)	Percent change, June 30, 1972 to June 30, 1973					
		Other consumer goods paper					Personal loans
		Total	Auto	Mobile homes	Credit cards and check credit	Other	
United States	70,727	19	19	34	24	19	14
Seventh District	9,604	18	17	39	28	14	11
SMSAs:							
Illinois							
Bloomington	38	15	13	15	43	0	3
Champaign	56	13	8	26	*	59	7
Chicago	2,171	17	19	65	30	-16	7
Decatur	61	20	16	24	50	39	57
Peoria	141	14	17	43	17	6	4
Quad Cities	112	18	19	80	25	22	10
Rockford	108	16	17	55	-87	63	1
Springfield	96	24	20	39	64	-21	10
Indiana							
Anderson	31	12	14	39	33	14	2
Ft. Wayne	156	42	46	47	20	88	30
Gary-Hammond	145	22	20	140	-50	23	8
Indianapolis	560	28	19	127	29	46	2
Lafayette	47	8	2	26	22	159	-20
Muncie	31	4	5	38	7	27	-5
South Bend	111	35	31	47	20	26	53
Terre Haute	67	25	24	40 ^e	*	45 ^e	19
Iowa							
Cedar Rapids	48	12	11	-2	29	38	3
Des Moines	126	26	27	82	51	62	5
Dubuque	25	7	7	42	0	15	13
Sioux City	40	25	18	20	*	35	-4
Waterloo	29	14	21	39	*	24	-9
Michigan							
Ann Arbor	83	6	22	19	52	-5	5
Detroit	1,388	22	22	30	32	28	37
Flint	202	16	34	84	30	-1	8
Grand Rapids	213	29	14	42	17	23	21
Jackson	63	19	22	17	15	55	30
Kalamazoo	107	24	26	85	28	90	30
Lansing	404	21	23	-6	26	28	87
Muskegon	35	36	33	181	29	-5	40
Saginaw	94	22	17	20	50	11	8
Wisconsin							
Green Bay	46	15	20	35	24	89	-5
Kenosha	19	28	24	20	50	26	0
Madison	90	13	15	3	27	13	16
Milwaukee	369	15	11	79	32	48	83
Racine	42	33	40	73	83	73	11

* Not computed due to small base amount.

^ePartly estimated.

Note: The Bay City, Michigan area data are not published to avoid disclosure of individual bank figures.

these areas became specialists in this type of financing as the industry developed, and they have made mobile home loans on a nationwide basis. National demand for mobile homes is, therefore, an important factor affecting their expansion.

As an indicator of this demand, total shipments of new mobile homes to all U.S. dealers increased approximately 10 percent for the year ending June 30, 1973 according to data published by the Mobile Home Manufacturing Association. Shipments to dealers in the five district states actually declined about 5 percent, however. In the same period, the average wholesale price of a new mobile home unit increased by 10.5 percent, reflecting in part a shift toward larger units. Given the rise in prices of both new mobile homes and conventional houses, increased demand for used mobile homes may have affected the growth of these loans. ■

Member bank operating ratios

Profitability of large district member banks was lower in 1973 than in 1972, while, in the same period, profitability of small banks was greater. The 1973 ratios of net income to equity capital ranged from an average of 10.3 percent for banks in the over \$500 million deposit-size group to 12.2 percent for banks in the \$10-25 million group. The average for all member banks was 11.7 percent. These and related ratios of Seventh District member banks are presented in *Operating Ratios*, an annual publication of the Federal Reserve Bank of Chicago. The ratios are arithmetic averages of individual banks' ratios. Individual bank ratios are computed from data reported in the Consolidated Report of Income for 1973, and averages of Consolidated Reports of Condition for December 1972 and June and December 1973.

The effects of high short-term interest rates in 1973 account for most of the variation in changes in profitability. Ratios of interest paid on time and savings deposits to total time and savings deposits averaged 5.12 percent for all district members in 1973—an increase of 39 basis points from 1972; the average for the largest banks (deposits greater than \$500 million) increased 121 basis points to 5.92 percent, reflecting increases in rates paid on certificates of deposit in denominations of \$100,000 or more. Further, interest on borrowings and capital notes and debentures, which had absorbed 8.57 percent of operating income at the largest banks in 1972, absorbed 14.60 percent of income in 1973. This large increase is traceable to heavier use of short-term borrowings, including purchases of federal funds and sales of securities under repurchase agreements, coupled with high short-term interest rates. On the other hand, high interest rates boosted the income of the banks that sold federal funds, particularly those in deposit-size groups under \$25 million. For banks in these size groups, 1973 ratios of interest and fees on loans to gross loans averaged at least 100 basis points higher when adjusted to include interest on and amounts of federal funds sold and securities purchased under agreements to resell.

At the "average bank," interest and fees on loans accounted for 65.78 percent of operating income in 1973, compared to 62.75 percent the previous year. The major expense item, interest on deposits, absorbed 43.78 percent of operating income, and salaries and employee benefits absorbed 19.06 percent. Since three-fourths of district member banks have deposits of less than \$50 million, average ratios for all members are influenced considerably by these banks. ■

