Do Farm Lenders’ Attitudes and Risk Assessment Models Encourage Organic Farms’ Debt Aversion?

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The 2004 survey conducted by the nonprofit Center for Community Self-Reliance revealed that 46% of organic farmer respondents considered debt as not necessary. For similar farms, this percentage is 30%. The lenders who do not really understand their farms (The Carrot Project, 2008).

The survey instrument contained questions on issues raised in two focus group discussions with organic farmers from different parts of Georgia held at Fort Valley State University and University of Georgia in 2002. Majority of study sample lending institutions are commercial banks (95.8%). The rest of the respondents consist of Farm Service Agency lending offices (7.4%) and lending associations under the Farm Credit System (7%).

32.4% of the survey participants had $10 million to $20 million in total assets during the fiscal year covered. On the other hand, 25.4% of the respondents had less than $2 million in total assets.

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The lenders’ extent of loan exposure has been analyzed using backward stepwise regression. The general form of the original model is

\[ Y_i = \beta_0 + \beta_1 X_{i1} + \beta_2 X_{i2} + \beta_3 X_{i3} + \beta_4 X_{i4} + \beta_5 X_{i5} + \epsilon_i \]

where
- \( Y_i \) is the dependent variable of interest.
- \( \epsilon_i \) is the error term.
- \( \beta_0 \) is the intercept.
- \( \beta_1, \beta_2, \beta_3, \beta_4, \beta_5 \) are the coefficients of the independent variables.

The results show that, relative to FSA and FCS lenders, commercial banks are less inclined to lend to organic farms.

In terms of credit risk assessment practices, lending institutions that do not consider assigning some premium to farmers’ soil enhancement investments are more likely to accommodate organic farmers’ loan applications. Lenders who put a premium on the risk-educating effects of enterprise diversification are more inclined to lend to organic farms. Moreover, institutions that employ a homogenous credit scoring (or credit risk assessment) models for different types of borrowers are more likely to lend to organic farmers.

The majority of the participating institutions in the survey (87.7%) have been in the business for more than 20 years.

RESEARCH OBJECTIVES

To validate the issues raised by organic farmers on their experiences in accessing regular farm credit. The lenders’ actual lending patterns and experiences, in addition to their perceptions of organic farms, will be analyzed and compared with the findings from the above survey.

To identify issues that can be emphasized in efforts to bridge the gap between organic farmers and near-term credit markets. Improving farmers’ access to credit will realize the potentials of business expansion opportunities in such a dynamic, growing farm sector.

RESEARCH METHODOLOGY

I. Data Source

The results of a regional farm lenders’ surveys conducted by the University of Georgia in 2002 among lending offices of commercial banks, the Farm Credit System, and the Farm Service Agency in Georgia, Florida, Alabama, South Carolina, North Carolina, Mississippi, Louisiana, Kentucky, Arkansas, and Tennessee.

II. Analytical Model

In this model, the dependent variable \( Y \) is the total amount of real estate and non-real estate loans granted by lending institutions to organic farm borrowers. The list of independent variables include: \( ST \) which is a set of lenders’ structural characteristics, such as size of operations, years of lending experience, type of institution; \( ATT \) are dummy variables accounting for lenders’ qualitative perceptions of organic farms, such as their attitudes towards organic farms (0, if lender does not really understand their farms; 1, if otherwise); \( Divergeffctdum \), \( Findisadrnk \), \( Envhlthrnk \) are dummy variables capturing the organic farms’ credit risk conditions.

Lenders that do not really perceive organic farms as sustainable, self-reliant operations tend to hold higher loan amounts to organic farms. In addition, lenders that recognize the significant differences of economic and precautionary measures of organic farms compared to conventional farms have expressed interest in accommodating organic farms’ loan applications.

RESEARCH CONCLUSIONS

This research has produced important evidence on the determinants of lenders’ differential treatments of organic and conventional farm borrowers. Results show that differences in qualitative perceptions of organic farmers and disparity in credit scoring models for different types of borrowers, property appraisal approaches that affect valuation of organic farmland, and other specific credit risk assessment benchmarks have effects on the chances of organic farm borrowers for both having their loan applications approved as well as for securing a higher loan amount. Kremen’s (2001: Adoption of more appropriate credit risk assessment models that should more accurately capture the organic farms’ credit risk conditions.


REFERENCES