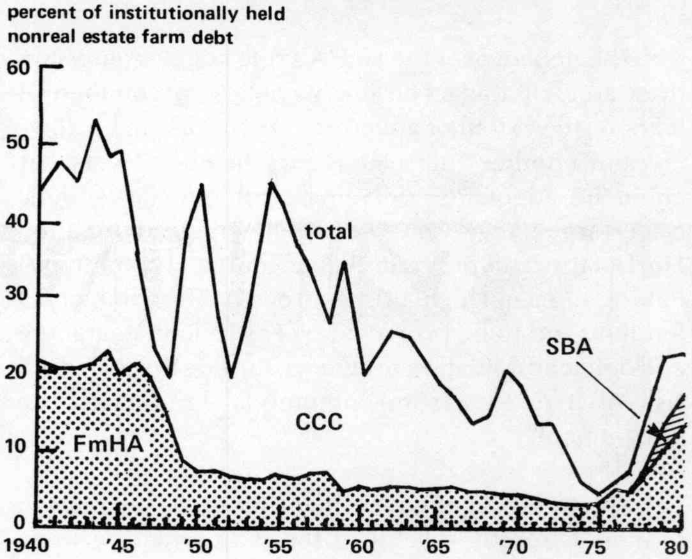
FEDERAL RESERVE BANK OF CHICAGO
AGRICULTURAL LETTER
ISSN 0002 - 1512
October 3, 1980 Number 1535

THE ROLE OF GOVERNMENT AGENCIES IN AGRICULTURAL LENDING has expanded sharply in recent years. USDA figures show that the three government agencies that lend to farmers—Commodity Credit Corporation, Farmers Home Administration, and Small Business Administration—accounted for nearly a fourth of all nonreal estate farm debt owed to institutional lenders at the beginning of this year, up from a low of 5 percent in 1975. The share held by banks over the past five years dropped to 47 percent from 62 percent, while the share held by PCAs dropped to 28 percent from 32 percent.

Share of nonreal estate farm debt held by government agencies has risen sharply



The share of institutionally held nonreal farm debt owed to government agencies, although the highest since the early 1960s, is not high by earlier standards. However, the mix of nonreal estate debt among government agencies has changed markedly. The share held by the CCC has risen in recent years, but remains well below pre-1973 levels. CCC credit to farmers is largely a by-product of the government's commodity price support programs. The recent increase in the CCC's share reflects a rebuilding of grain stocks and—at times—a liberal credit program that encouraged farmers to build grain storage facilities.

The FmHA and—since 1977—the SBA have accounted for most of the increased government agency lending to farmers. Following an elevenfold increase in outstandings, the share of institutionally held nonreal estate farm debt owed to the FmHA and the SBA has risen from 3.5 percent in 1975 to more than 17 percent at the beginning of this year. That is the largest share for the FmHA and its predecessor agencies since the 1940s, an era when the FmHA's share was swelled by post-depression programs adopted by Congress to relieve the financial plight of farmers.

FmHA lending to farmers is carried out through several programs. The more traditional "farm operating" and "farm ownership" programs have experienced significant growth in recent years. But most of the growth in FmHA and SBA lending has come through various emergency and disaster loan programs. In fiscal 1979 such programs accounted for 80 percent of the funds extended to farmers by the FmHA and 90 percent of the funds extended by the SBA. Emergency and disaster lending by the FmHA is certain to register further large gains this year. The statutory ceiling for the FmHA's Economic Emergency Loan Program was raised from $4 billion to $6 billion earlier this year. Half of the increase has already been extended to farmers and there is little doubt the remainder will be before the program's scheduled expiration in September 1981. Moreover, lending through the FmHA's Emergency (disaster) Loan Program will be very large because of widespread losses from this year's drought. This program has no statutory ceiling on obligations. It is available to farmers who suffer a loss of 20 percent or more as a result of a natural disaster. Under this program loans to cover actual losses, up to a maximum of $500,000, are available at 5 percent interest.

Debate over the proper role for government agencies has increased with their rising share of the agricultural credit market. Most of the debate concerns the FmHA. Although not immune from the debate, the question of CCC lending is more complicated because of its ties to commodity price support programs, particularly the three-year grain reserve program. Concern about the SBA's role has diminished because of recent legislation that is expected to virtually remove the SBA from farm credit markets. The legislation requires farmers who seek emergency loans to apply first at the FmHA rather than the SBA. This change, however, increases the potential exposure for the FmHA, particularly since the "credit-elsewhere" test for FmHA emergency lending has been relaxed to accommodate creditworthy farmers who previously qualified for SBA disaster loans.

The debate over the FmHA's role largely centers on three areas: its impact on lending policies of commercial lenders, the extent of government subsidies to borrowers, and whether the FmHA is attracting borrowers that could be adequately served by commercial lenders. Many argue that Congress's willingness to broaden FmHA farm loan programs has encouraged commercial lenders to accept higher risk borrowers. The commercial lenders tend to be protected by FmHA loan guarantee and debt consolidation programs, shifting the increased risk of loan loss from commercial lenders to the government.

The question of government subsidies on loans to farmers is mostly related to the differential between interest rates on FmHA loans and rates charged by commercial lenders. At times in the recent past, the rapid growth in government agency lending to farmers was supported by low interest rates. Except for disaster loans to cover actual losses, interest rates on most FmHA farm loan programs are now tied to the government's average cost of funds. Most FmHA farm loan rates now range from 10½ percent to 12½ percent. Although the subsidies implied by such rates are not inconsequential, the extent of the interest rate subsidy is considerably less than at times in the past.

Those who argue the FmHA is attracting farm borrowers who should be served by commercial lenders question the restrictiveness of the FmHA's "credit-elsewhere" test, particularly in light of the large loans extended to some FmHA borrowers. (Except for the recent changes in the disaster loan program, the eligibility requirements of most FmHA farm loan programs stipulate that the borrower has to be unable to obtain credit from normal lenders.) Until recently, there was no restriction on the maximum loan to an individual borrower in the disaster loan program. Many believe the recently imposed ceiling of $2 million ($500,000 to cover actual losses and $1.5 million for adjustment and operating credit) is inordinately high for a viable borrower who supposedly is unable to obtain credit from commercial lenders. Individual loan ceilings for other FmHA farm loan programs are $400,000 for Economic Emergency Loans, $200,000 for farm ownership loans, and $100,000 for farm operating loans. In many agricultural areas, these ceilings are probably well in excess of the norm for many commercial borrowers.

Congressional debate on new legislation to succeed the farm bill that expires next year is certain to address the question of the government's role in financing agriculture. In a sense, it is ironic that the government's role has expanded so sharply in a decade in which farm income, although variable, has been high and the appreciation in land values has been unparalleled. At the same time the government's expanded role reflects genuine Congressional concerns about saving the family farm, supporting beginning farmers, and protecting farmers from abnormal hardships. These concerns will still be evident next year. As is often the case, however, limiting government program benefits to targeted objectives is not easy. This is the real issue that Congress and the Administration will hopefully settle next year.

Gary L. Benjamin

HOG PRODUCTION continued to decline this summer. According to the USDA's latest *Hogs and Pigs* report, the June-August pig crop was down 10 percent from a year ago. Smaller pig crops this spring and summer have resulted in lower inventories of market hogs as of September 1. The inventory of breeding animals is also down, portending a reduction in farrowings this fall and winter. Hog slaughter may match year-earlier levels in the fourth quarter but will likely be sharply lower in the first half of next year. Hog prices may temporarily decline but could recover strongly in the first half of next year.

The smaller pig crop in 14 states reflected the reduction in sows farrowed this summer. Farrowings were down 10 percent from the year before, a slightly larger decline that the intentions indicated in June. The average number of 7.2 pigs saved per litter was unchanged from a year ago, but still below the historical average. Compared to spring, the June-August seasonal decline in farrowings was the largest in six years.

The downturn in farrowings is expected to continue in the months ahead. Producer intentions for September-November point to 10 percent fewer sow farrowings than the year before. For the December-February period, producers intend to reduce farrowings by 7 percent.

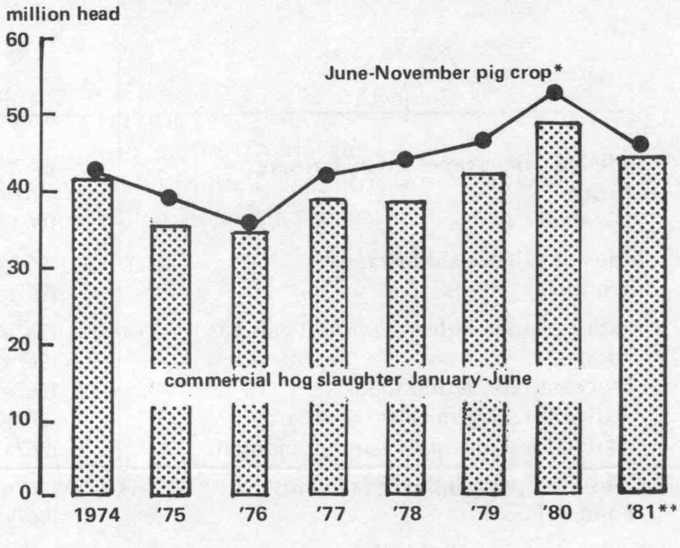
Hog inventories remain high, although down from a year ago. As of September 1, the inventory of all hogs and pigs—at 55.6 million—was 3 percent below last year. The inventory of breeding animals was 10 percent below the cyclical peak reached September 1, 1979. Market hogs numbered 2 percent less than a year ago but 15 percent more than in 1977 and 1978. This summer's high temperatures apparently caused slower weight gains and contributed to a proportionately large inventory of heavyweight hogs. The inventory of larger market hogs (180 pounds and over) was 9 percent higher than a year ago, whereas that for pigs under 60 pounds was down 9 percent.

Hog producers in district states followed the 14-state pattern with some exceptions. Percentage declines in summer farrowings in Illinois, Indiana, and Wisconsin approximated the 14-state average, but in Iowa farrowings were off only 5 percent from the year before. Intended farrowings for September-November are relatively higher in three of the district states. However, Indiana producers intend a 17 percent reduction in sow farrowings this fall. Three of the states—Illinois, Iowa, and Wisconsin—reported lower inventories of market hogs than the year before. In Iowa producers held more market animals.

Hog slaughter set a record for the first half of 1980. The January-June slaughter was up 18 percent from a year ago. Third-quarter slaughter declined seasonally from the second quarter and based on preliminary estimates was unchanged from the same period a year ago. Earlier projections pointed to a 5 percent to 7 percent year-to-year increase in third-quarter slaughter. Slow weight gains during the hot summer months apparently contributed to the less-than-expected marketings this summer.

The high inventory of heavyweight market hogs on September 1 suggests fourth-quarter slaughter will rise seasonally and may equal the record set a year ago. In the first half of next year, however, hog slaughter is likely to be well below the first-half level of this year. The estimated 10 percent decline in this summer's pig crop and the indication that producers intend to cut farrowings by a similar amount this fall suggests that first-half

Smaller pig crop signals lower hog slaughter



*In previous year.
**Estimate.

1981 hog slaughter may be down a tenth. Despite the decline pork supplies would still be fairly high with respect to most earlier years.

Hog price increases since May have markedly improved the profit picture for producers. Barrow and gilt prices have recently ranged from $46 to $48 per hundredweight. Break-even for farrow to finish operators is currently estimated at $42 by Iowa State analysts. This spring hog producers were losing about $10 per hundredweight when hog prices dipped to a six-year low.

In the fourth quarter hog prices may temporarily fall below the mid-$40s if the high slaughter indicated by the larger inventory of heavyweight hogs occurs. Subsequently, prices may average in the upper $40s as slaughter drops below year-earlier levels in the first half of 1981.

Production of other meats is not expected to be a detrimental factor. Beef and poultry production is expected to hold equal to or below year-ago levels in the fourth quarter and not to increase appreciably in early 1981. On the other hand, prospects for a sluggish economy and only limited gains in real disposable income may depress consumer purchases of meat, particularly in light of the recent increases in pork, beef, and poultry prices at retail. Retail pork prices alone have risen 20 percent from the May-June low of this year. In early September the retail price of pork averaged $1.52 per pound, up from $1.36 a year ago.

Jeff Miller

Selected agricultural economic developments

Subject	Unit	Latest period	Value	Percent change from	
				Prior period	Year ago
Index of prices received by farmers	1967=100	September	261	+ 2.0	+ 9
Crops	1967=100	September	258	+ 3.2	+14
Livestock	1967=100	September	263	+ 0.4	+ 4
Index of prices paid by farmers	1967=100	September	286	+ 1.1	+12
Production items	1967=100	September	282	+ 1.4	+11
Producer price index* *(finished goods)*	1967=100	August	249	+ 1.0	+15
Foods	1967=100	August	245	+ 2.3	+10
Processed foods and feeds	1967=100	August	249	+ 3.3	+13
Agricultural chemicals	1967=100	August	260	+ 0.5	+21
Agricultural machinery and equipment	1967=100	August	259	+ 0.6	+11
Consumer price index** *(all items)*	1967=100	August	249	+ 0.6	+13
Food at home	1967=100	August	256	+ 1.9	+10
Cash prices received by farmers					
Corn	dol. per bu.	September	3.03	+ 3.8	+21
Soybeans	dol. per bu.	September	7.69	+ 7.1	+13
Wheat	dol. per bu.	September	3.97	+ 0.8	+ 3
Sorghum	dol. per cwt.	September	5.22	+ 2.0	+23
Oats	dol. per bu.	September	1.63	+ 6.5	+26
Steers and heifers	dol. per cwt.	September	68.30	– 1.2	– 3
Hogs	dol. per cwt.	September	45.80	– 0.9	+23
Milk, all sold to plants	dol. per cwt.	September	13.10	+ 2.3	+ 7
Broilers	cents per lb.	September	32.1	+ 1.9	+40
Eggs	cents per doz.	September	61.9	+ 6.7	+12
Income *(seasonally adjusted annual rate)*					
Cash receipts from farm marketings	bil. dol.	2nd Quarter	132	– 0.8	+ 1
Net farm income	bil. dol.	2nd Quarter	22	–15.4	–33
Nonagricultural personal income	bil. dol.	August	2,093	+ 0.8	+10

*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

DR.E.FRED KOLLER A3
UNIVERSITY OF MINNESOTA
DEPT.OF AGRIC.ECONOMICS
UNIVERSITY FARM
ST.PAUL,MINNESOTA 55101