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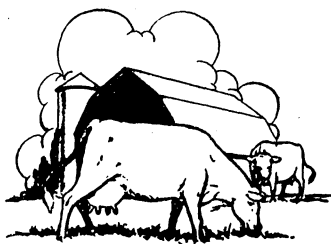
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MINNESOTA farm business NOTES



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Better Credit Policies Needed in Supply Co-ops

Arvid C. Knudtson and E. Fred Koller

Half of the farm supplies sold by a cross section of Minnesota farm supply associations in 1953 was sold on credit.

A survey of credit trends and practices in 87 representative farm supply associations has revealed this serious credit problem now facing cooperatives. The problem is on the increase, too. For example, the oil associations studied made 58.5 per cent of their supply sales on credit in 1953 compared to 52.5 per cent in 1950.

The associations studied, which sold \$24 million of farm supplies in 1953, included 46 grain, 32 oil, and 9 general supply associations.

Outstanding accounts increased 58 per cent for the 87 associations while sales increased only 8 per cent from 1950 to 1953. The average volume of receivables increased from \$12,242 per association in 1950 to \$19,420 in 1953.

In addition, the proportion of total assets in receivables has been increasing (see table 1). For oil associations the proportion of assets in receivables increased from 10.8 per cent in 1950 to 13.2 per cent in 1953. In grain associations this ratio increased from 7.4 per cent to 9.5 per cent over the four years. Increasing receivables means less money for business expansion or current obligations.

An excellent measure of the effectiveness of credit policy is that of days'

credit sales in receivables. This figure is arrived at by dividing accounts receivable by the average daily credit sales. Days' credit sales in receivables should be less than 30 days where the terms are "net 30 days."

Average days of credit sales in receivables for the 87 associations increased from 41 in 1950 to 51 in 1953. The fact that this average is high and going higher suggests the need for attention to credit extension and collection. The credit situation of grain and oil associations was less favorable in 1953 than in 1950 while that of supply associations improved slightly (see table 2).

Table 2. Average Number of Days' Credit Sales in Receivables in 87 Minnesota Farm Supply Associations, According to Type, 1950-1953

Associations		1950	1951	1952	1953
Type	Number	number of days			
Grain	46	49	59	58	64
Oil	32	34	39	40	42
Supply	9	44	48	44	39
All types	87	41	48	48	51

The longer an account is outstanding, the greater the probability of loss. Table 3 shows that in 51 associations for which the information was available, only 39 per cent of the total receivables was within the 30-day terms. For a sub-group of 38 of these associations an average of 9 per cent of the receivables was over one year old.

The costs involved in extending credit and collecting accounts often are not fully realized by those handling or using credit. These costs include interest on the capital tied up in receivables, extra clerical and accounting costs, collection expenses, and bad debt losses.

In 1953 the average cost of extending credit was found to be \$1.92 per \$100

Table 3. Per Cent of Accounts Receivable of 51 Minnesota Farm Supply Associations in Various Age Groups, According to Type, 1953

Associations		Under 30 days		Over 6 mos.		Total
Type	Number	30 days	to 6 mos.	per cent		
Grain	16	49	36	15		100
Oil	27	33	48	19		100
Supply	8	38	44	18		100
All types	51	39	44	17		100

of credit sales in the associations surveyed. Even though credit costs are relatively low at present, there is cause for concern because these costs are based on a period of favorable farm income when less time is spent on credit work and bad debt losses are low. It is anticipated that the present high volume of credit sales and receivables may cause credit costs to rise in the period ahead.

Supervision of credit extension was in the hands of the manager in almost all the 87 associations. In some associations the board of directors occasionally handled credit approvals. In a few cases a credit committee was appointed to review and approve credit requests. One-third of the oil associations authorized their bulk oil deliverymen to extend credit within prescribed limits.

Managers generally were not held financially responsible for credit losses. The exceptions were nine oil associations and two grain associations. Fifteen per cent of the oil associations allowed their deliverymen to extend credit and held them financially responsible for it.

The extent of financial responsibility varied as did the means of recouping losses from employees. The two most common methods were (1) to charge employees with 10 to 100 per cent of the losses on accounts as they occurred

(Continued on page 3)

Table 1. Average Proportion of Total Assets in Receivables in 87 Minnesota Farm Supply Associations, According to Type, 1950-1953

Associations		1950	1951	1952	1953
Type	Number	per cent			
Grain	46	7.4	9.0	8.3	9.5
Oil	32	10.8	12.4	13.1	13.2
Supply	9	11.5	11.8	11.9	10.9
All types	87	8.9	10.4	10.1	10.8

DIRECT LOANS AND CONTRACTS FOR MACHINERY WEIGHED

R. P. Dahl and S. A. Engene

A large investment in machinery and equipment is required for modern farming. As of January 1, 1953, the value of farm machinery and motor vehicles on farms in the United States totalled \$17 billion.

Records from 300 successful southern Minnesota farmers in 1953 showed these book values:

	Total value	Value per acre of tillable land
Crop machinery	\$4,459	\$22
Tractors, trucks, farm share of auto	\$3,307	\$16

Records from the Red River Valley are similar. Original cost approximated twice the present book value for these farmers.

Farmers have provided some of the funds to purchase this machinery out of savings from farm income, but a considerable amount came from borrowing. The nonreal-estate debt of Minnesota farmers held by the principal lending agencies totalled \$178 million on January 1, 1953. A sizable portion of this was in machinery loans.

Country banks are the leading suppliers of machinery loans to farmers; banks currently hold about 80 per cent of the nonreal-estate farm debt in Minnesota. Production credit associations are also important sources of machinery loans. These lending agencies have about 10 per cent of the nonreal-estate farm debt.

Farmers who wish to borrow to purchase machinery obtain their funds in two principal ways: (1) they may borrow directly from a lending institution such as a bank or production credit association, or (2) they may borrow by buying their machines on conditional sales contracts. The latter frequently is an indirect form of borrowing from a bank because the dealer may sell this contract to a bank.

There is no clear-cut answer to the question as to the best type of loan, but a study made by the Department of Agricultural Economics of the University of Minnesota revealed several points.

Bankers in 57 country banks estimated that about 37 per cent of their nonreal-estate farm loans were for the purchase of farm machinery. Bankers also estimated that about 30 per cent of their total machinery loans represented con-

tracts purchased from dealers. The remainder were direct machinery loans.

Direct Loan Often Means Lower Interest

One advantage of a direct loan is that interest may be less. With direct loans bankers usually charge simple interest; after a payment has been made on the principal, future interest is charged on only the remainder. On contracts, however, the interest may be calculated in advance and applied to the entire principal of the loan.

Calculating interest in advance may mean paying twice as much interest. To illustrate, take a loan for \$1,200 to be repaid in 12 monthly installments at 6 per cent interest. If the interest is paid each month on the balance, the total payment of interest will be \$39. However, if the interest is charged in advance on the entire principal, the total interest charged will be \$72.

Calculating the interest charge at 6 per cent in advance is actually about equal to charging 12 per cent on the funds actually used.

Most machinery contracts are repaid in two or more irregular installments—not monthly payments. However, when interest is calculated in advance on installment contracts, the amount of interest is always higher than if simple interest is charged.

About one-third of the banks that purchased dealer contracts reported that interest was calculated in advance. The stated rate varied from 4½ to 7 per cent, with 6 per cent being the most common. The other two-thirds of the banks carried contracts on the basis of simple interest at 6 to 8 per cent.

The banks reported 6 per cent simple interest as the most common interest rate on direct machinery loans. Twenty banks reported this rate. Sixteen banks indicated that they charged 7 per cent. A number of banks reported that the interest rate varied.

Direct Loan Means Better Bargaining, Better Understanding

A second advantage of a direct loan is that the farmer may be in a stronger bargaining position if he comes to the dealer with prearranged financing. Cash usually speaks for itself. A direct loan also enables him to buy more conveniently from several dealers.

Third, it may be an advantage for the farmer to get his machinery loan

from the same place he obtains other production credit. A contract, on the other hand, may be sold to another bank that is not so familiar with the farmer and his business.

Since the major purpose of machinery is the enhancement of farm earnings through more efficient production, machinery credit should be treated as an integral part of the farmer's production credit borrowings. If the farmer obtains all his production credit direct from one lending agency, he will be in a better position to watch the character and size of his nonreal-estate debts. In addition, the lender will be in a better position to provide the needed credit.

Direct Loan Means Farmer Gets Title

Finally, when the farmer uses a direct loan to purchase a machine, he gets title to that machine. This is true despite the fact that he may pledge the machine as security for the loan in a chattel mortgage.

A contract, on the other hand, does not give him title to the machine. The lender consequently has the privilege of repossessing the machine without resorting to legal action if payments on the contract are not met. As a debtor, the farmer is in a stronger position if he has title to the equipment.

Contracts Have Advantages, Too

One advantage of conditional sales contracts is that they may give the farmer a longer repayment period. In fact, 31 banks reported that contracts that involved major equipment such as tractors, combines, and field choppers were made for terms from one to two years or over two crop years. On the other hand, the terms of direct loans are often restricted to six months or one year. Although these loans are usually made with an understanding of renewal if needed, nevertheless the farmer is in a less secure position when he must rely on a renewal.

Adjusting the loan term to the time of anticipated farm income is desirable for both contracts and direct loans.

On the average, the down payment requirements on contracts were somewhat lower than on direct loans. Most banks requested a down payment of one-third of the purchase price on direct loans, while down payment re-

DIRECT LOANS AND CONTRACTS FOR MACHINERY WEIGHED

Continued from page 2

quirements on contracts were commonly one-fourth to one-third of the purchase price. The fact that the down payment was smaller, however, may be offset by the fact that title to the machine is not obtained and larger amounts must be paid later.

Assigning relative weights to the advantages of contracts and direct loans is difficult, but the advantages of direct loans probably outweigh those of contracts for most farmers.

To reduce financing costs the farmer must start by planning his purchases. Since he is buying machinery to increase his earnings, before buying he must be certain that the benefits exceed the costs.

Each farmer should do some careful figuring for each machine he buys. Some average figures will be helpful, however. Records obtained from 30 southern Minnesota farmers in 1951 and 1952 show the following average costs per farm:

	Tractors	Crop machinery
Depreciation	\$253	\$ 478
Interest	80	162
Repairs and upkeep	174	165
Servicing (value of own labor)	32	138
Fuel and oil	434	9
Shelter	16	94
Total	\$989	\$1,046

Depreciation is a very large part of these costs. But since this depreciation is set when the farmer buys the machine, he can plan before he buys. Careful operation can, of course, extend the life of the machine, reduce other costs, and help reduce needs and costs for financing.

The most important place to watch machinery costs is in buying harvesting machines; in general, they are the most expensive. Here are the average costs of various types of machines for the farmers mentioned above:

MINNESOTA

farm business

NOTES

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Hauling and general machinery	\$ 213
Tillage machinery	160
Planting and cultivating machinery	121
Harvesting machinery	530
Crop sprayer	22
Total	\$1,046

There is no fixed rule for determining whether or not a farmer can afford to buy a given machine. He must figure it for each machine.

If costs are high, the farmer may be able to reduce them by (1) hiring the work done, (2) buying in cooperation with neighbors, (3) buying a second-hand machine, (4) doing custom work, or (5) doing the work with other machinery.

BETTER CREDIT POLICIES NEEDED IN SUPPLY CO-OPS—Continued from page 1

or (2) to retain a percentage of their commissions and salaries for the purpose of establishing a reserve for credit losses. This reserve ranged from 33 to 100 per cent of the outstanding receivables. Accounts that were written off against an employee's reserve became the property of the employee.

In 52 of the associations new credit applicants were "screened" on the basis of their past credit record, reputation, capacity, and willingness to pay. Information was obtained by interviewing, checking references, and using local credit bureaus. A total of 35 of the 87 associations did not check the past credit performance of credit applicants.

The time to start collecting an account is at the time of sale, according to the managers in 33 of the 87 associations. They indicated that agreement on terms of repayment at time of sale was the most helpful method in collecting accounts.

All of the associations used statements of account as a method in aiding collections. The frequency with which statements were sent to patrons varied from every 30 days in most associations to only once a year in a few cases.

Collection letters were used by 48 of the 87 associations. A few used collection letters when an account became

60 days past due. Many waited until an account was clearly inactive before using letters.

The practice of making personal collection visits was used in 65 of the 87 associations. There was general agreement among the managers of these 65 associations that personal contact often was successful where other collection methods failed.

Special collection services—usually local credit bureaus or local attorneys—were used by 55 of the 87 associations. The fees charged for this service varied between one-third and one-half of the account. This is expensive, but experience shows that collectors generally recoup much of what would otherwise be completely lost.

Credit business can be profitable if it is transacted with good credit risks and within the framework of a sound credit policy. It was found that only 30 associations out of the 87 were operating on a definite credit policy established by the board of directors. In the other 57 associations no policy had been set by the board or the policy the board had set was not being followed. Many of the 57 associations indicated that the manager set the credit policy.

The most common types of credit policies found included (1) 30-, 60-, or

90-day credit terms, (2) cash discounts in 10 days, (3) 30 days plus 5 or 6 per cent interest after 30 days, (4) individual dollar limits on accounts, and (5) a "one-fill" system used by a few oil associations.

The picture of rising receivables presented above points to the need for improving credit policies. In planning an improved credit policy the following suggestions may be of value.

- Patrons should receive a written statement of the policies to be followed in granting credit and making collections.

- The patrons, as well as the management and directors, should understand that it is not the function of a supply association to take care of the farmers' seasonal credit needs.

- Patrons should be assisted in obtaining the credit they need from specialized credit institutions.

- The accounting procedures of the associations should permit checking of individual accounts at monthly intervals.

- There should be close supervision by the management.

- The board of directors must assume the responsibility of seeing that the manager and employees carry out the credit policies which are adopted.

Minnesota Farm Prices, For June - July 1954

Prepared by Jerry M. Law

Average Farm Prices for Minnesota,
June and July 1954,
With Comparisons*

	June 1954	June 1953	July 1954	July 1953
Wheat	\$2.12	\$2.11	\$2.15	\$2.07
Corn	1.38	1.30	1.38	1.30
Oats .....	.71	.65	.63	.67
Barley	1.07	1.14	1.03	1.09
Rye .....	.88	1.18	.96	1.13
Flax	3.56	3.35	3.23	3.21
Potatoes .....	.75	1.00	1.00	1.00
Hay	14.80	15.80	15.60	14.20
Hogs	19.50	21.90	19.20	22.30
Cattle	17.40	17.60	16.90	18.20
Calves	17.50	18.70	17.70	19.00
Sheep-lambs	19.55	20.13	18.09	20.13
Chickens .....	.156	.203	.130	.209
Eggs .....	.270	.425	.280	.425
Butterfat .....	.62	.71	.62	.71
Milk	2.85	3.25	2.95	3.35
Wool† .....	.50	.51	.50	.49

* Average prices as reported by the USDA.

† Not included in the index numbers given below for Minnesota.

The indexes of Minnesota farm prices represent the average of the increases and decreases in farm product prices in the given month of 1954 over the average of the five corresponding months of 1935-39.

Weights for the Minnesota indexes are the average sales in the five corresponding months of 1935-39. Weights for the United States indexes are the average sales of 60 months in 1935-39.

Prices received by Minnesota farmers in July averaged slightly below those of the previous month. Primarily responsible for the lower average were price declines for flax, cattle, hogs, oats, and chickens. Potatoes, milk, eggs, rye, and calves increased in price.

The Outlook Corner - The Broiler Situation

The broiler business is revolutionizing poultry meat production, and even further changes can be expected.

Only 12 per cent of the poultry meat in the United States came from commercial broilers in 1935-39; most of the meat came from cull hens, from cockerels, and from cull pullets produced as farmers raised a laying flock. But by 1953 almost 64 per cent of poultry meat came from commercial broilers.

The per capita consumption of chicken was 17.9 pounds per year in 1935-39. This increased to 29.4 pounds in 1953. During the same period consumption of turkey increased from 2.6 to 5.0 pounds, while consumption of red meats rose from 125.3 to 153.7 pounds.

Not only has poultry meat increased in quantity, but it also makes up a larger proportion of all meats. In 1935-39 chicken meat made up 12.6 per cent of all meat; by 1953 this had increased to 16.4 per cent. During the same period turkey meats increased from 1.3 per cent to 3.2 per cent of all meats.

Among factors responsible for these changes are—

1. Improved breeding.
2. Improved housing.
3. Use of labor-saving devices.
4. Improved feeding.
5. Large reductions in death losses.
6. Improved processing.
7. Improved packaging.
8. Improved refrigeration.

Further improvements along these lines can be expected, along with further increases in poultry meat consumption and more emphasis on broiler production.

Commercial broiler production has not been developed extensively in Minnesota. In 1953 it accounted for only 12 per cent of all poultry meat production in the state, as compared with 64 per cent for the nation. Several factors have been responsible:

1. We must ship the refrigerated product a long way to reach the big population centers. We do, however, have an advantage for our local market.

2. Minnesota farmers have ample supplies of feed, but they have many other profitable uses for their feed and labor.

3. Egg production has fitted well with other enterprises as part of a diversified farming system; broiler production tends to conflict with other enterprises and consequently tends toward specialized production.

It is probable that market outlets for good poultry meats will continue to expand if high-quality meat is sold in an attractive manner.

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Indexes and Ratios for Minnesota Agriculture

	June 1954	Average, June 1935-39	July 1954	Average, July 1935-39
U. S. farm price index	235.3	100	231.3	100
Minnesota farm price index	222.1	100	215.6	100
Minnesota crop price index	232.2	100	220.8	100
Minnesota livestock price index	239.9	100	231.8	100
Minnesota livestock products price index	204.4	100	199.6	100
Purchasing power of farm products United States	104.6	100	103.7	100
Minnesota	98.8	100	96.7	100
Minnesota farmers' share of consumers' food dollar	57.2*	45.5	56.2†	48.4
U. S. hog-corn ratio	14.6	12.0	14.6	12.3
Minnesota hog-corn ratio	14.1	15.2	13.9	14.6
Minnesota beef-corn ratio	12.6	12.8	12.2	12.0
Minnesota egg-grain ratio	9.5	14.6	10.0	15.9
Minnesota butterfat-farm-grain ratio	27.2	30.9	29.0	33.5

* Figure for February.

† Figure for March.

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