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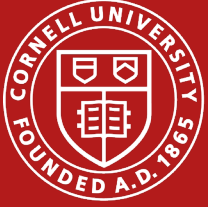
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# Nontraditional Finance in U.S. Agriculture

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# What is nontraditional finance?

“Nontraditional credit suppliers or lenders...are those whose primary contacts with producers historically have been for goods and services other than credit” (Sherrick, Sonka, & Monke, 1994)

Traditional finance	Nontraditional finance
   	         <p data-bbox="1375 985 2216 1071">Farmland Partners Announces Loan Agreement with Rabo AgriFinance Company Release - 12/18/2017 4:05 PM ET</p>

My definition: lenders working outside of the (“traditional”) local branch-loan officer model

## 2 stories about nontraditional finance

### Financial distress

- Lender of last (second?) resort
- “Financial bridge to struggling farmers”
- “Prolonging the agony and potentially building up [farm] losses instead of cutting the pain, cauterizing the wound and stanching the flow of financial blood now”

<https://www.wsj.com/articles/farmers-in-crisis-turn-to-high-interest-loans-as-banks-pull-back-11573381801>

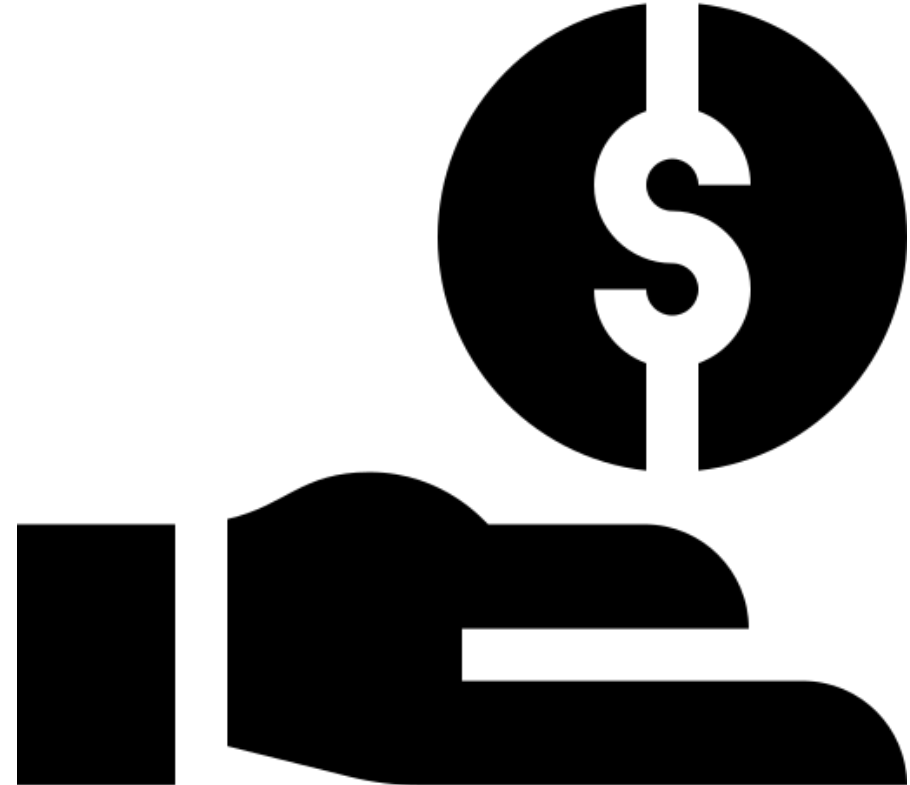
<https://www.wsj.com/articles/americas-farmers-turn-to-bank-of-john-deere-1500398960>

### Modern agricultural credit markets

- Almost everyone that \*sells something\* to farmers sells credit too
- Increasing competition
- Segmentation
- Differentiation by:
  - Convenience
  - Service
  - Bundling
  - Standards
  - Source of collateral

## Ag lending 101

- Requires
  - Overcoming serious information barriers (moral hazard)
  - Collateral \*and\* the ability to collect collateral
- Not “easy money”
  - Competitive market facing same risks as production agriculture



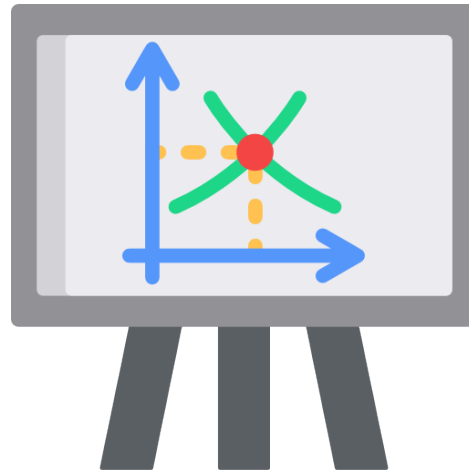
# What drives the growth in nontraditional finance?

## Supply side factors

- Outside capital
- Innovation
- Lending standards

## Demand factors

- Financial stress
- Diverse U.S. farm business
  - Large and small
  - Complex
  - Fast-growing
  - Increased appetite for risk?



# Nontraditional lenders rival largest Farm Credit lenders

- Farm Credit Services of American: **\$28.4** billion loan volume in 2018
- Farm Credit Mid-America: **\$20.9** billion loans (owned) in 2018
- Metlife: **\$19.4** billion agricultural loan portfolio (Sept 30 2019)
- Compeer: **\$18.7** billion net loans in 2018
- Rabo Agrifinace: **\$15** billion loan volume reported in 2019 (estimate, not based on regulatory reports)
  - Rabobank N.A. had **~\$4.7** billion in non-real estate & real-estate ag production loans on Dec. 31 2018
- Deere Financial: **\$2.4** billion in non-real estate ag loans on Dec. 31 2018
- Farm loans holdings of the **largest 30** U.S. banks declined **17.5%** between Dec 2015 and March 2019 (**\$18.3** billion held in March 2019)
- 2020 USDA farm sector debt forecast: **\$425** billion

<https://www.fcsamerica.com/about/newsroom/financial-reports>

<https://e-farmcredit.com/getmedia/aeed4072-21d0-43ec-8e1b-56f78dc733a5/2018-Annual-Report.pdf.aspx>

[https://www.compeer.com/getattachment/Utility/Support/About/Financials/Financial-Reports/722918-Compeer-2018-Annual-Report-\(1\).pdf.aspx?lang=en-US](https://www.compeer.com/getattachment/Utility/Support/About/Financials/Financial-Reports/722918-Compeer-2018-Annual-Report-(1).pdf.aspx?lang=en-US)

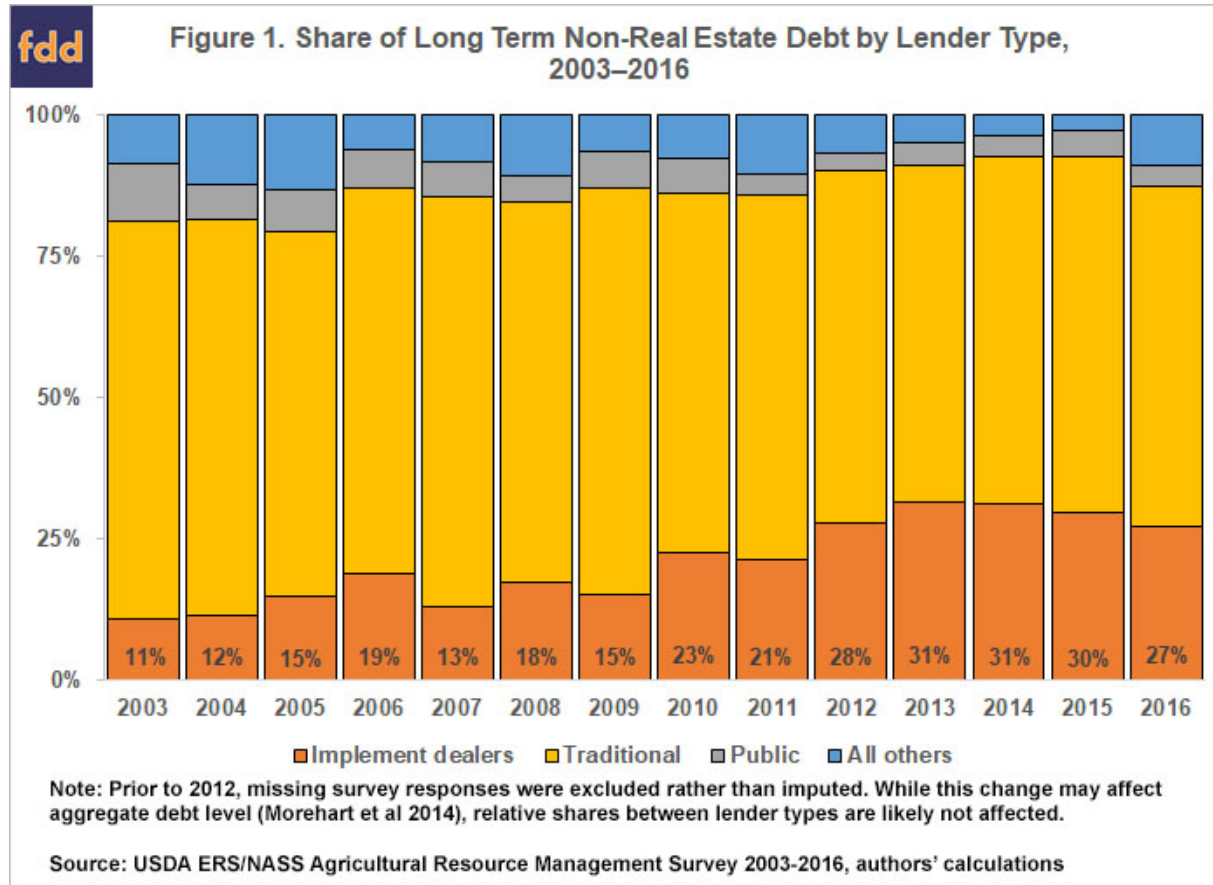
<https://www.bankingdive.com/news/rabobank-us-agriculture-lending-gap/559142/>

<https://investments.metlife.com/financing-solutions/agricultural-finance/>

<https://www.reuters.com/article/us-usa-farmers-lending-insight/wall-street-banks-bailing-on-troubled-u-s-farm-sector-idUSKCN1U618F>

<https://www.ers.usda.gov/topics/farm-economy/farm-sector-income-finances/highlights-from-the-farm-income-forecast/>

# Implement dealer-financing has gained market share



It is challenging to directly learn much more about nontraditional lenders from USDA farm survey data

Source: Kuethe, Ifft, and Patrick (2018)



# Some nontraditional finance providers have competitive interest rates

- Interest rates not consistent across type of nontraditional lender
  - Can be higher, same, or lower
- Commercial farms report better rates *in general*
  - 92 basis points
- Implement dealer financing may be more competitive for smaller farms
  - 52 vs 3 basis points
- But what about input costs?

Average **equipment\*** interest rates and loan volume, 2012-2016

**Table 1: Average interest rate and loan size by sales class and lender type, 2012-2016 average**

	Low sales farms	Moderate sales farms	Midsize farms	Small million dollar farms	Large million dollar farms
Traditional	4.75%	4.74%	4.63%	4.38%	3.83%
Implement dealers	4.23%	4.28%	3.94%	3.98%	3.80%
Public	3.39%	3.61%	3.81%	3.65%	4.55%
All others	4.76%	4.40%	4.32%	3.89%	3.72%
Traditional	\$35,929	\$94,035	\$156,735	\$300,930	\$1,293,482
Implement dealers	\$39,284	\$95,154	\$138,515	\$206,850	\$452,403
Public	\$36,427	\$80,639	\$117,815	\$172,721	\$1,252,160
All others	\$31,674	\$141,427	\$134,720	\$211,444	\$740,652

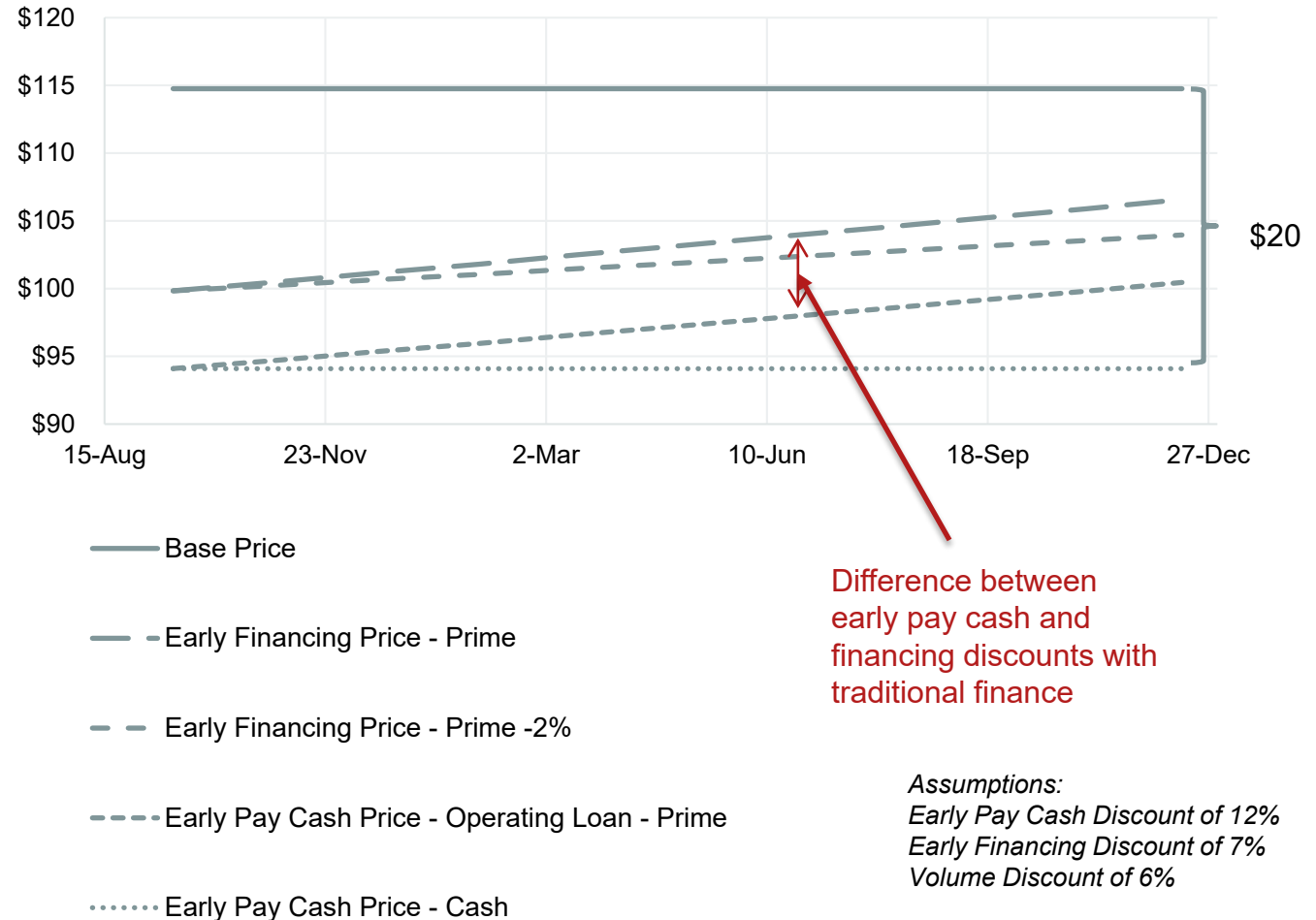
*Source: USDA ERS/NASS Agricultural Resource Management Survey 2012-2016, authors' calculations*

\*Non-real estate long term loans, typically equipment or machinery  
 Source: Ifft, Kuethe, and Patrick (2018)

# Vendor credit may come with higher effective input costs

- Cash price often lower than effective financed price
- Seed corn discount case study
  - Due to loss of early cash pay discount, promotional financing will usually be more expensive than 'traditional financing'

**Seed Corn Price with Financing Options**  
Cost/Acre - \$270 per bag price



Fiechter & Ifft, *farmdoc daily* series, October 2019

# Nontraditional finance and farm financial stress



Bridge

OR



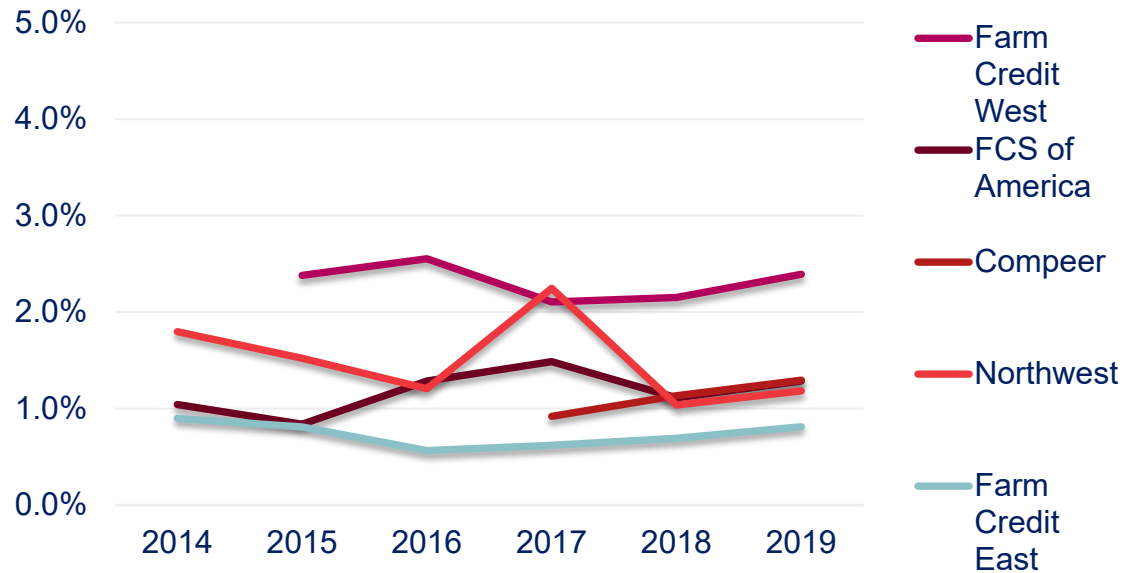
Off-ramp?

Source <https://www.democratandchronicle.com/story/news/2016/12/09/its-a-wonderful-life-seneca-falls-george-bailey-frank-capra/94825632/>  
<https://www.bizjournals.com/albany/news/2019/07/12/exit-3-northway-changes-commute-albany.html>

# Risk profile varies regionally and by institution

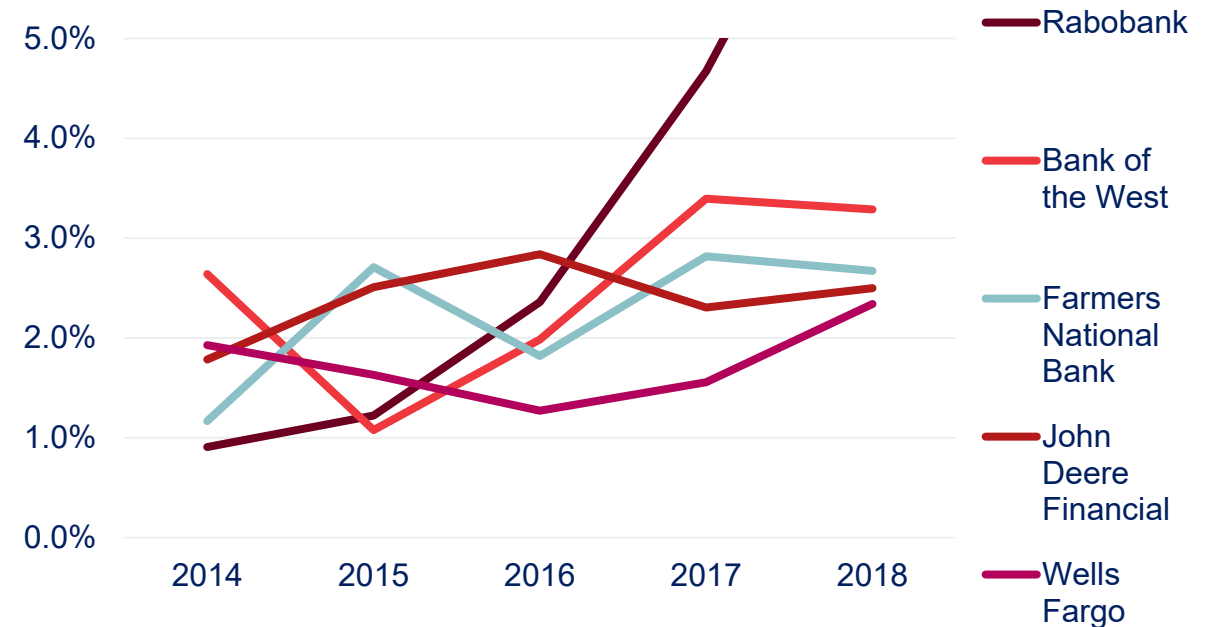
## Farm Credit System Lenders

### Delinquencies and Charge-offs



## Commercial Banks

### Delinquencies and Charge-offs



# Nontraditional finance is not necessarily related to farm stress

For implement financing: no observable differences

**Table 1. Share of Farms with Long-Term Non-Real Estate Debt and Experiencing Potential Financial Stress by Lender Type, 2012-2016**

	<b>Solvency</b> D/A ratio > 50%	<b>Liquidity</b> Current ratio < 1	<b>Profitability</b> Net cash income < 0	<b>Repayment Capacity</b> Debt coverage ratio < 1
<b>Implement Dealer</b>	15%	48%	41%	44%
<b>Traditional</b>	14%	44%	42%	44%

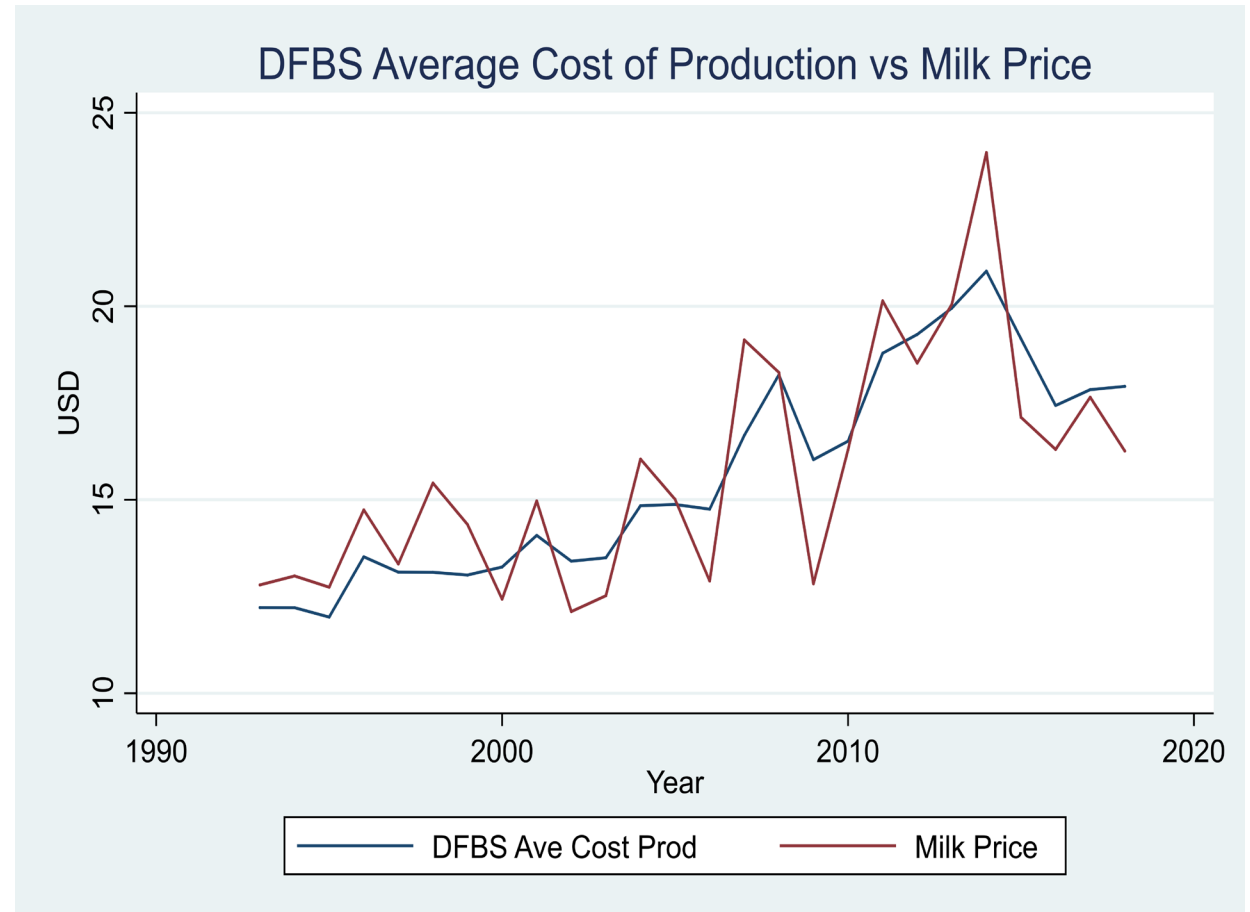
Note: Traditional lenders include commercial banks, Farm Credit System lenders, credit unions, and Farmer Mac.

Source: USDA ERS/NASS Agricultural Resource Management Survey 2012-2016, authors' calculations

Source: Patrick, Kuethe, and Ifft (2018)

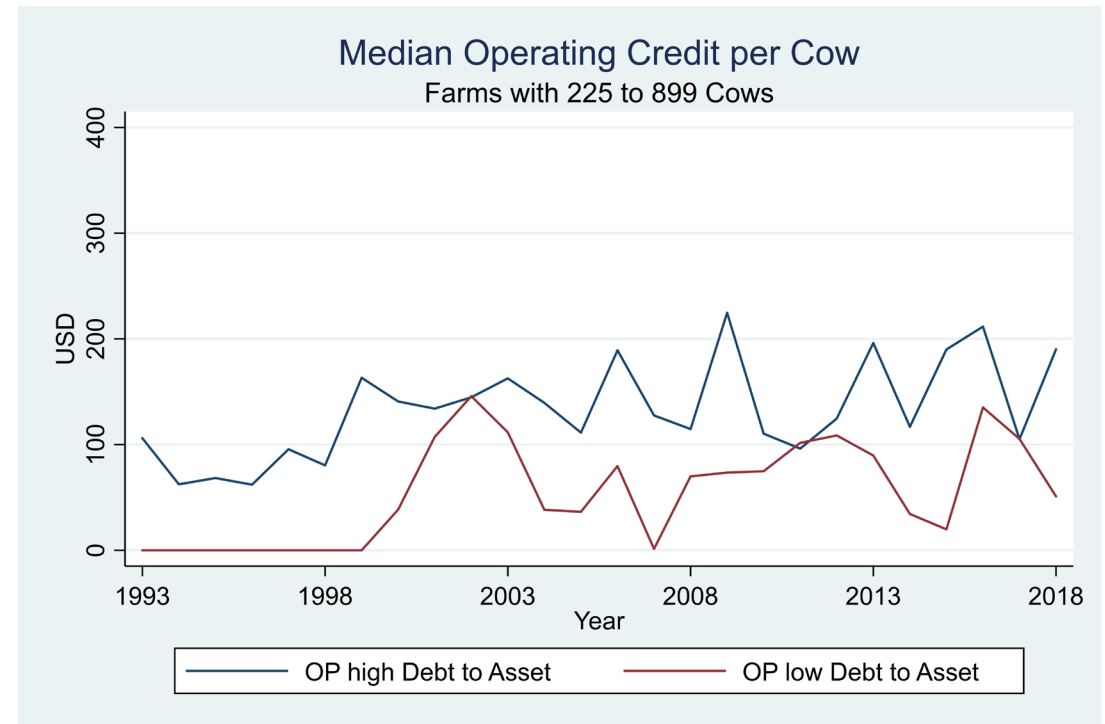
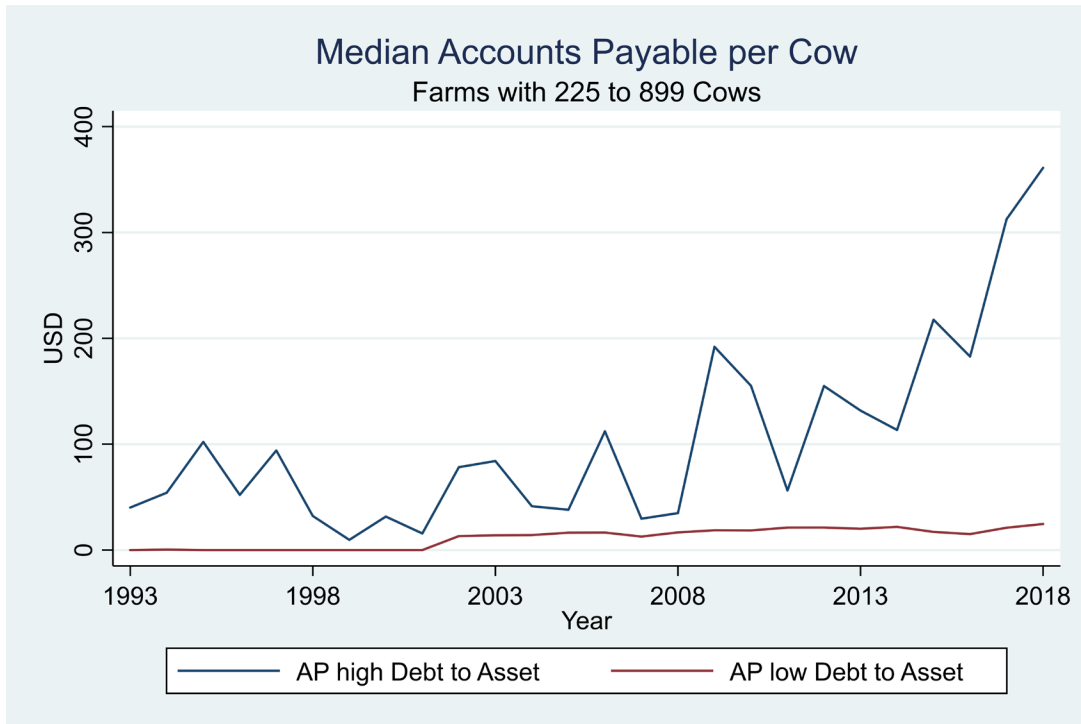
# NE Case Study: financial stress and milk prices

- Partnership with NEAFA
- Feed manufacturer accounts receivable
  - >70% of market
  - Delinquencies ~4x higher than Farm Credit East, ~3x higher than Deere Financial
  - Loan volume equivalent to large community bank with multiple branches
- 25 years of dairy farm survey data
  - Long-term countercyclical relationship of accounts payable & milk prices
  - More so in recent years, for midsize, higher-leveraged farms



Source: Fiechter and Ifft, 2019; Data: Cornell Dairy Farm Business Summary

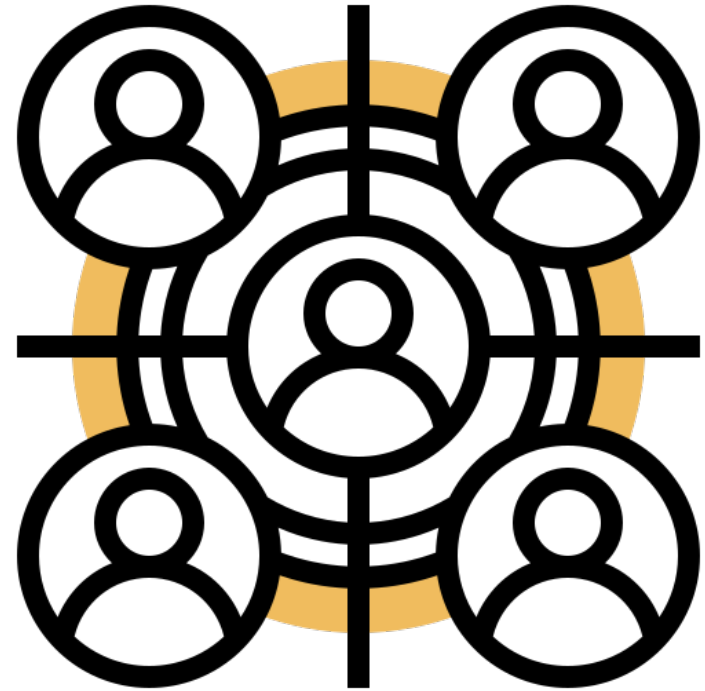
# NE case study: vendor financing plays important role during periods of financial stress



Source: Fiechter and Ifft, 2019; Data: Cornell Dairy Farm Business Summary

## Takeaways: nontraditional lenders....

- Create additional value and risk in agricultural credit markets
- Make farm management more interesting
- May partially be motivated by strategies to maintain or increase market share (applies to vendor credit)
- Make tracking financial stress in agricultural more challenging





## Open questions

- Bridge or off-ramp? Can be yes to both, but not the whole story
- Do vendors/suppliers fully account for downside and collateral risk?
  - Vendor partnerships with nontraditional lenders growing
- Does “who gets paid first” matter?
- Does financial regulation developed post-80s farm crisis make sense today?
- How to measure and track farm debt from nontraditional sources?
  - Bellwether for farm stress?

## References and resources

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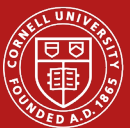
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