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FUTURE SOURCES OF LOANABLE FUNDS FOR AGRICULTURAL BANKS

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Commentary

Dale Stansbury

John Lee's paper makes many valid points and raises several unresolved issues that I want to consider briefly. In order to put the discussion in perspective, the first issue that I will consider is John's statement, "There is not a specific, articulated national policy on farm credit."

It is true that we do not have a document entitled, "National Agricultural Credit Policy," but we do have a national food and agricultural policy which contains a well developed credit component. Our policy in the simplest terms is to ensure adequate food and fiber at reasonable prices while ensuring that farmers have fair returns. In order to achieve these ends, we have a long-standing policy that farmers need access to adequate credit at reasonable terms.

Our policy views credit as a tool, with the objective being agricultural production. The policy generally takes a neutral attitude toward who makes the loans, and for this reason does not directly address the more narrow focus of this Symposium—Future Sources of Loanable Funds for Agricultural Banks. However, our national agricultural credit policy does affect loan fund availability, and some programs have uneven effects on various lenders. So, as I discuss the paper, I will try to relate the general policy to the bank funds question.

Historic Development

In response to economic distress in agriculture, uncertainty of credit supply, and inadequate terms for the credit that was available, all three national parties—Democratic, Republican, and Bull Moose—included an agricultural credit plank in their 1912 party platforms. This was translated into legislation with the passage of the Farm Loan

Act in 1916. In addition, the Federal Reserve Act included some special provisions for agricultural lending.

The Farm Loan Act is the predecessor of the Farm Credit System. However, there was no provision for delivery of production credit in the original Act. Banks and other existing institutions were expected to carry out the credit delivery and to use the Federal Intermediate Credit Banks for discounting. However, the agricultural depression of the '20s was so severe that the credit problems of farmers worsened and bankers never picked up their discounting option.

In 1933, the Consolidated Farm Credit System was established, and new authority was provided for Production Credit Associations. While this action did not exclude banks from the FICB discount window, it did result in 50 years of animosity between banks and PCA's.

Two other actions started with the New Deal are of importance to agricultural credit. First, there was the Resettlement Administration, which would ultimately evolve into the Farmers Home Administration. The early object was to resettle poor people from cities on farms and, with passage of the Bankhead Jones Farm Tenant Act in 1935, it broadened its effort to provide farm-ownership opportunities, especially for farm tenants. The other action is probably of greater consequence for agriculture credit — enactment of the Agricultural Adjustment Act. The subsequent stability of agricultural prices and income has been very important to the growth and development of our agricultural credit system.

However, the credit programs and underlying farm policy initiatives languished until the economy turned around with the advent of World War II. In fact, takeoff by the Farm Credit System didn't occur until the late '60s, and FmHA has only recently shown a sharp increase in lending.

One brief aside. I don't believe that agricultural credit is the principal determinate of the technological transformation of agriculture. Credit is an important lubricant in that it eases and facilitates, but it is not a causual factor in itself. The expansion of demand, economic recovery, and improved and stabilized agricultural incomes, starting with the war effort, caused the technological change. These same factors also stimulated the growth and development of agricultural credit in this country.

Current Situation

The keynote paper by Peter Barry has very capably described the current situation, so I want to look at only two points — off-farm income and shifts among lenders.

I have some problems with John Lee's discussion of off-farm income. The breakout of farms with sales of $2,500 or less is in my mind an extraneous matter to commercial credit for agriculture. Any agricultural credit policy discussion can concentrate on farms with $40,000 or more. There are financial service needs by rural residents, but in most cases these are not agricultural credit needs. In many cases, we are dealing with social problems whose inclusion in credit discussions is a disservice to both issues. Second, John's discussion of off-farm income to service agricultural debt would seem to be an internal subsidy that could result in misallocation of resources just as John says a public subsidy does. I believe off-farm income is a legitimate consideration for loan officers in making loans, but not for overall agricultural credit policy.

The recent shifts in market share of agricultural credit show the Farm Credit System becoming more dominant, banks barely holding their own or slipping, and government lending for production credit growing sharply. The reasons are fairly obvious. The Farm Credit System has fund access and is a single-purpose lender—agriculture. I don't see them having any price advantage since farm credit interest rates are often higher than those of other lenders. Their advantages lie in access to funds and singleness of purpose.

The bank problem is lack of funds and, perhaps more importantly, expanding opportunity for fund use. The improvement in the money market makes it easier for funds to flow away from rural banks than for rural banks to attract funds. Also, rural bankers are not a homogeneous group all of whom are dedicated to lending to agriculture. Most are good businessmen who find it more logical to invest in secure T-bills at 18 per cent than to deal with uncertain farm loans at 15 per cent.

The surge in FmHA lending for production is troublesome and raises questions about our system. However, if you look more closely, this surge is for emergency credits of one type or another going back to the Emergency Livestock Credit Act of 1974. During the drafting of that Act it was sometimes facetiously referred to as the Bankers' Relief Act. I would suggest that this Act and the subsequent Economic Emergency Credit Act have relieved agricultural lenders

—banks as well as the Farm Credit System—of many problem loans. The more important question is what the Federal program is being used for rather than its size. However, let me also say that the viability of support institutions is critical to our agricultural well-being. I'm asking, how much help should there be?

John raised several interesting side issues about agricultural credit including misallocation of resources, overuse of capital in agricultural, over-production, land inflation, and the fact that credit abets concentration. Dozens of books and conferences have been devoted to these issues. There is no way to fully discuss these issues here. However, permit me to state that the market, our tax policies and stabilization programs, plus the fact that the rich have an advantage in a market economy are more important in these developments than credit policy.

I began by suggesting that our principal policy is to ensure that agriculture has adequate credit. I personally believe that agriculture will be able to attract the credit it needs and, further, will be able to pay the going rate. The question is the role of banking in the future of agricultural credit. In all likelihood the Farm Credit System will become more dominant. Fewer banks will be able to provide adequate credit to meet farmers' needs because of their size, fund limits, and competing demands for loans.

Correspondent banking relationships can't fill the gap. These arrangements are too inefficient and individualized to serve the demand. However, I do think that banks need and must have better access to the FICB discounting. Again, the national objective is service to agriculture, not institutional glorification. Both sides must recognize that they can be complements rather than pure competitors. Further, those farm credit loans usually end up as bank deposits—as loanable funds for banks. I want to point out that nonagricultural rural America has a more serious credit deficit than does agriculture. It is imperative that rural banks service this need, because there is no alternative.

The questions about Federal subsidies and Federal loan programs will resolve themselves. The problem of the budget deficit is increasing accountability for all spending programs. We are already seeing this in the case of tightened standards for the Economic Emergency Program, failure to achieve highly subsidized rates for CCC storage loans, and a reduced role for SBA in agriculture. Given time, even government can be logical, and I'm sure that our agricultural credit system will evolve to serve national needs.