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AGRICULTURAL FINANCE: OUTLOOK FOR 1972

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Agricultural Finance: Outlook for 1972

Credit is one of the most important tools a farmer has. It has been that way for centuries and will remain so. While we are concerned with the whole subject of the financial condition of farmers, the major thrust of this discussion will be on farm credit--short-, intermediate-, and long-term loans. How much will be needed this year, where will it come from, and how much will it cost?

In a nutshell, the answers come out about like this: More credit will be used this year than any year so far--about 7 percent more than last year which was also a record. Farm loans will be available from the usual sources--banks, PCA's, Federal land banks, life insurance companies, FHA, merchants, individuals, and other miscellaneous lenders--with the main difference being the more active participation by life insurance companies. The interest rates will be close to those of last year. The total cost, though, will be up by 6 or 7 percent because of the increase in amount used. With the larger money supply, most farmers will be able to get the credit they want. However, in some distress areas such as Aroostook County, Maine, farmers who are now excessively in debt may have trouble getting more credit.

It's not unusual that farmers will use more credit in 1972. In fact, some of our friends say they always can predict our outlook every year: "More credit will be used than a year earlier." The records show that farm debt has increased every year since 1946.

Also of significance is the accelerating rate of increase. Beginning in 1946, it took 10 years for total farm debt to increase $10 billion, the next $10 billion increase required 6 years, and to add the last $10 billion it took less than 3 years. One could say that is a rapid rate of increase by most any kind of measure.

Debt, however, does not tell the whole story. Much farm credit, especially operating credit is obtained and repaid during each year. The total amount of operating credit used during a year is estimated to be almost double the amount outstanding at the beginning of the year. To explain, at the beginning of 1972 non-real estate farm debt outstanding was about $35 billion. Adding $29 billion estimated to be borrowed and repaid during the year, we see that farm operating credit actually used in 1972 will amount to about $64 billion. When combined with farm real estate debt of $31 billion the total farm credit used in 1972 will be close to $95 billion, compared with only $65.5 billion outstanding at the beginning of the year.

Even in these days of astronomical dollar figures, $95 billion is still a chunk of money. To highlight it a little, it is equal to two-fifths of the Federal budget for fiscal 1972, four-fifths of the total Federal personal and corporate income taxes due for 1972 and one-fifth more than the whole Federal defense budget for 1972. Before we get to feeling too good about how much credit farmers can muster, we note these same relationships were true back in 1965. But the big difference is, in 1972 we will have credit use of $95 billion compared with about $52 billion used in 1965, with the $95 billion debt being shouldered by 500,000 fewer farm operators farming 30 million fewer acres of land than in 1965.

Credit Uses

To go back to the expected increase in use of farm credit in 1972, it is reasonable to ask, why the increase and for what purpose? Perhaps of most importance is that farmers are basically optimistic. And this year they may be more willing than usual to borrow to become more efficient or to meet higher costs. Gross farm income is headed upward this year with net farm income expected to increase about $1-1/2-2 billion. That translates to a $600 or better gain in net income per farm.

Interest rates are still too high to expect a boom in farm long-term lending, but farm mortgage lending is expected to increase due in part to farmers refinancing short-term debts that were incurred for purposes usually calling for long-term loans. Capital improvements and farm enlargement, in many cases postponed the last 2 or 3 years, will create additional debt.

Building and equipping livestock feedlots, although only a small part of the total, will require increased financing. Maybe not this year but likely within the next couple years, many livestock farmers will be installing waste disposal facilities at substantial costs--much of which they will probably have to bear themselves with the aid of long-term loans.

Farm operating costs are continually increasing. The proportion furnished by borrowing also continues to increase. Total acres of crops planted in 1972 are expected to be 2 or 3 percent below last year. However, acreages of some crops will increase. Cotton and soybeans are among the more important. Cotton is a high-cost crop compared with other major row crops. Soybeans, although not expensive to grow, do require expensive machinery and equipment. Even a drop of 4 percent in corn acreage, as intended by farmers in a survey as of January 1, would not decrease the total expense outlay for that crop by much.

Money going into livestock ranch and feedlot operations in 1972 will likely increase over 1971. Cattle feedlots are expected to increase placements over 1971 and operate nearer capacity. Feeder cattle will likely remain relatively high priced throughout the year. While the number of feeder pigs fed will remain under 1971 numbers, prices for feeder pigs will probably remain high most of the year.

Machinery and equipment bought to replace worn-out or obsolete items will cost more than last year. Although price controls may help slow the price rise, some increase is inevitable. Other expense items such as fertilizers, fuels, labor and repairs will also increase. All of these expense items will call for additional sums of borrowed money.

Loan Sources

Where will the loans come from? With the exception of more lending by life insurance companies than in 1969-71, the sources of farm loans will be the same as for the past decade or so. In farm mortgage lending, Federal land banks, life insurance companies, and banks will be the main suppliers. Individuals and other miscellaneous lenders regularly furnish about a third of farm mortgage credit.

Banks and production credit associations furnish the bulk of farm short- and intermediate-term credit. Farmers Home Administration, merchants, dealers, and individuals provide about two-fifths of the total. Much of the merchant and dealer credit is probably refinanced later into bank or PCA loans.

There have been a few recent changes in sources of farm credit. Federal land banks, in 1969, became the major farm mortgage lender, and PCA's are rapidly gaining on banks as the major farm non-real estate lender. It is too early to tell what effect the Farm Credit Act of 1971 will have on farm lending by the Farm Credit Banks.

As mentioned earlier, interest rates on farm loans in 1972 will probably change little from levels reached last summer. Even at that, though, rates of 7 to 8 percent and over on farm mortgage loans are high historically and close to levels which may not permit reasonable profits on many heavily indebted farms.

As a typical example, consider a farmer obtaining an 80 percent loan to buy $500 per acre farmland on terms of 30 years at 7.5 percent interest. At least for the first several years of the loan, he will incur an annual cash interest expense of about $30 per acre. At present prices that amounts to about 25 bushels of corn, 10 bushels of soybeans, or 100 pounds of lint cotton per acre. And, that doesn't include any part of the principal sum that has to be repaid.

The total annual interest bill for farm loans amounts to a sizable figure. In 1971 it was about $3.8 billion. For 1972 it is estimated to total about $4.1 billion. Total interest charges on farm loans in recent years have been about 11 percent of annual total farm production expenses.

Loan Quality

With farm debt increasing more rapidly, what about the quality of farm loans and the state of farmers' financial condition? According to lenders and others responding to our survey last fall, farmers generally were servicing their debts without difficulty. Most farmers were able to handle their 1971 debt obligations satisfactorily, including some who had debt carryover from 1970. Cash receipts from farm marketings were $2.4 billion larger in 1971 than in 1970, although government payments declined about $1/2 billion. Both cash receipts from farm marketings and government payments are expected to increase this year. Nonfarm income of farmers and members of their households is expected to increase. So, in all but a relatively few distressed areas, farmers would be able to handle their indebtedness in 1972 and in the foreseeable future.

While the vast majority of farmers handle their debts satisfactorily, there are always some who for some reason or other do not. There are indications that loans running into repayment problems are averaging larger in size than was the case several years ago. As an example, in the second quarter of 1964, 1970 and 1971, new farm mortgage loans made by life insurance companies averaged $32,000, $74,000, and $80,000 respectively. Their farm loans in process of foreclosure on June 30, 1964, and 1970, and 1971 averaged $20,000, $102,000, and $171,000 respectively. Although the difference between new loan size and size of loans in process of foreclosure is not as wide with Federal land banks as with life insurance companies, the same situation exists. Even though farm mortgage loans in trouble represent only a minor part of the total, the significant point is they are averaging much larger size than the average loan outstanding. Although there is more statistical evidence for farm mortgage loans than for non-real estate loans, the situation appears to be the same with non-real estate farm loans.

The equity position of farmers is still judged to be sound by our survey respondents, although some pointed out that the debt to asset ratio was steadily increasing. Nationally the farm debt to asset ratio has increased steadily over the past 20 years, from 9.4 percent in 1950 to 18.8 percent in 1970 and 19.5 percent at the beginning of this year. Since as many as a third of the farms have no debt, of course, the debt to asset ratio of indebted farms would be substantially higher, but still low enough to evidence a healthy financial position for American agriculture.