Credit Access of Organic Farms: A Survey on Agricultural Lending Institutions in Southeast Region

Hofner D. Rusiana and Cesar L. Escalante
Department of Agricultural and Applied Economics
The University of Georgia

INTRODUCTION

The booming organic farming sector registered an accelerated pace of growth in recent years; however, organic farmers have been unable to match the pace of market expansion with increases in their farm production (Dimitri and Oberholtzer, 2009). The expansion and growth of the industry hinge on the availability of borrowed capital, among other options, to supplement existing funds to finance larger operating infrastructure and working capital requirements.

Credit access is a critical issue for organic farmers as sufficient funding allows businesses to survive and grow. However, agricultural lending institutions have traditionally tailored their financial services after the needs of large conventional farming systems. It is possible that lenders could be inclined to shun away from accommodating (relatively “too retail”) businesses of smaller or new farmers (to save on transaction costs), a category that includes most organic farms (Blank, 1998; USDA-ERS; Walz, 2004). As organic farms operate smaller operations, their credit requirements could be relatively smaller than the average loan requests of conventional farm businesses. When lenders factor in transaction costs that are incurred regardless of loan size, they prioritize the servicing of larger loan requests, rather than squander time and resources on smaller loan requests of some organic farmers.

Access to credit is one of impediments to the expansion and sustaining viability of organic farm businesses in the Southeastern region. In order to resolve operating constraints, increased access to credit is needed and will lead to business growth and expansion. As an effect, this leads to significant expansion of the organic farming industry in the region that will fill in the widening supply gap.

METHODOLOGY

A research project, funded by a grant from the Southern Sustainable Agriculture and Research Education (SARE), was implemented by agricultural economists from the University of Georgia and Fort Valley State University to determine farm lenders’ views, perceptions, and current practices that might affect the extent of credit access of organic farmers in the Southeast region. The survey was conducted among commercial banks, community banks, Farm Credit System associations and Farm Service Agency branches in the Southeast. The survey questionnaire gathered structural and operating characteristics of lending institutions as well as their perceptions of organic farming risks and their attitudes towards organic farm loan requests vis-à-vis their regular farm borrowers.

This survey was conducted in the latter half of 2012. The survey instrument was mailed to 2000 agricultural lending institutions in Alabama, Florida, Georgia, Mississippi, North Carolina, South Carolina, Louisiana, Kentucky, Arkansas, and Tennessee and Alabama. Of the lending institutions contacted, 68 responses were received, representing a response rate of 3.4%.

The following sections summarize the major findings of this survey according to the respondent's structural characteristics, as well as the recent access of both conventional and organic farmers on their institutions. [1]

A. RESPONDENTS' GENERAL PROFILE: STRUCTURAL CHARACTERISTICS

A.1 Types of Agricultural Lender

Question: *"What type of agricultural lender is your institution?"*

Type of Institution	Number	Percentage
Commercial Bank	37	56.9%
Farm Credit Association	5	7.7%
Farm Service Agency	23	35.4%
Total	**65**	**100%**

A.2 Agricultural Lenders' Asset Size

Question: ***"****During the last fiscal/calendar year, what was the estimated size (total assets) of your institution?"*

	Number	Percentage
Less than $100 million	15	25.4%
$100 million to $200 million	19	32.2%
$201 million to $500 million	11	18.6%
$501 million to $1 billion	5	8.5%
$1 billion to $2 billion	4	6.8%
$2 billion to $5 billion	0	0.0%
$5 billion to $10 billion	1	1.7%
Over $10 billion	4	6.8%
Total	**59**	**100%**

[1] Please be cautioned that certain response categories might contain missing observations as certain respondents could have skipped some questions.

A.3 Lending Experience (Years)

Question: *"How long has your institution been in the lending business?"*		
	Number	**Percentage**
Less than 5 years	0	0.0%
5 to 10 years	4	6.2%
10 to 15 years	2	3.1%
15 to 20 years	2	3.1%
More than 20 years	57	87.7%
Total	**65**	**100%**

A.4 Percent of Loans to Agricultural or Farm Sector

Question: *"On the average, how much did you lend to agricultural or farm borrowers (percent of total loans) during the last two years?"*		
	Number	**Percentage**
Less than 10%	18	29.0%
10% to 15%	9	14.5%
16% to 20%	3	4.8%
21% to 25%	2	3.2%
26% to 30%	3	4.8%
31% to 35%	2	3.2%
36% to 40%	3	4.8%
41% to 45%	1	1.6%
46% to 50%	0	0.0%
Over 50%	21	33.9%
Total	**62**	**100%**

The summary in table A.1 indicates that the majority of study's sample lending institutions are commercial banks (56.9%). Lenders from the Farm Service Agency (FSA) and Farm Credit System (FCS) comprised 35.4% and 7.7%, respectively, of the sample of survey respondents.

In terms of asset size (table A.2), about one-third of the lending institutions that participated in the study had $100 million to $200 million in estimated total assets during the 2012 fiscal year. On the other hand, 25.4% of the respondents had less than $100 million estimated total assets while 18.6% has total assets ranging from $200 to $500 million.

The summary in table A.3 shows that the majority of the participating institutions in the survey (87.7%) have been in the lending business for more than 20 years. The remainder of the sample had lending experiences of 15-20 years (3.1%), 10 to 15 years (6.2%) and 15 to 20 years (3.1%).

Table A.4 presents the extent of credit granted to agricultural borrowers account measured as a proportion of the lenders' total loan portfolios. The results indicate that 33.9% of the lending institutions extended farm loans accounting for over 50% of their total loan portfolios disbursed during the last two years. In contrast, 29% of the sample had less than 10% of their total loan portfolios devoted to farm credit.

B. ORGANIC FARMS' CREDIT ACCESS

B.1 Respondents' Past Lending Transactions with Organic Farm Borrowers

B.1.1 Lending exposure to organic farm borrowers

Question: *"On the average, how much did you lend to organic farm borrowers during the past several years?"*		
	Number	**Percentage**
Less than 1%	50	82.0%
1% to 5%	11	18.0%
6% to 10%	0	0.0%
11% to 15%	0	0.0%
16% to 20%	0	0.0%
21% to 25%	0	0.0%
25% to 50%	0	0.0%
More than 50%	0	0.0%
Total	**61**	**100%**

B.1.2. Growth in organic farm lending operations

Question: *"On the average, by how much did the number of your organic farm borrowers grow during the last two years?"*		
	Number	**Percentage**
No growth	51	83.6%
Less than 10%	8	13.1%
11% to 25%	1	1.6%
Greater than 25%	1	1.6%
Total	**61**	**100%**

As shown in table B.1.1, 82% of the respondents had minimal credit dealings with organic farm borrowers given their credit exposures of less than 1% of their agricultural loan portfolios during the past several years. The remaining 18% of the sample indicate that only 1% to 5% of their lending services to the agricultural sector were given to organic farms. This is a general indication that organic farmers only comprise a small percentage of the sample's lending exposure to the agricultural sector.

The interactions between the lending institutions and organic farms in the previous years have been minimal and have not improved in spite of the accelerated pace of growth registered by organic farming sector in recent years. As shown in table B.1.2, majority of the participating institutions in the survey (83.6%) state that the number of their organic farm borrowing clients did not grow during the last two years. However, 13.1% of the lending institutions indicate that they experienced some growth (less than 10%) in their dealings with organic farm borrowers. Only 2.6% of the respondents indicate that they had 11 percent and above increase in credit accommodations to organic farm borrowers during the last two years.

B.2 Respondents' Credit Dealings with Organic Farm Borrowers

B.2.1. Amount of real estate and non-real estate loans

Question: *"What is the AVERAGE AMOUNT of real estate and non-real estate loans requested by organic farm borrowers during the past year?"*

	Real Estate Loans	Non-Real Estate Loans	Response Count	
Less than $10,000	19	22	25	64.10%
$10,000 to $50,000	4	6	7	17.95%
$50,000 to $100,000	3	3	6	15.38%
$100,000 to $200,000	6	1	6	15.38%
$200,000 to $500,000	0	1	2	5.13%
$500,000 to $1 million	2	1	2	5.13%
Over $1 million	0	0	0	0.00%

Based on table B.2.1, more than half (55.88%) of respondents state that the amount of real estate loans requested by organic farm borrowers were less than $10,000. The non-real estate loans data also indicate the same trend where 64% of respondents had less than $10,000 loan request from organic farmers during the past year. Combining these two response categories, 64.1% of the participating institutions indicate that majority of the organic farm borrowers requested less than $10,000 for both loan types.

B.2.2. Maturity of real estate and non-real estate loans

Question: *"What is the AVERAGE MATURITY of real estate and non-real estate loans requested by (and funded for) organic farm borrowers during the past year?"*

	Real Estate Loans	Non-Real Estate Loans	Response Count	
Less than 1 year	12	13	14	41.18%
1 to 2 years	0	3	3	8.82%
3 to 5 years	7	13	14	41.18%
6 to 10 years	3	3	6	17.65%
11 to 15 years	3	0	3	8.82%
16 to 20 years	2	0	2	5.88%
More than 20 years	5	0	5	14.71%

Lending institutions were inclined to provide short term loans to organic farm borrowers. As shown in table (2), 37.5% of the respondents provided real estate loans to organic farm borrowers for a term of less than one year during the past year. Non-real estate loans for organic farms, on the other hand, had an average term of either less than 1 year or 3 to 5 years average maturity (both categories with 41% each of the sample). Considering both loan types, the average maturity of loans granted to organic farm borrowers was either less than 1 year or 3 to 5 years (both with 41.18% of the sample).

B.3 Respondents' Perception of Organic Farmers

B.3.1. Organic farm borrowers' chance obtaining a loan

Question: *"How likely would certain farm borrowers obtain a loan from your institution vis-à-vis other types of farm borrowers of the same credit risk and loan request?"*

	Uncertified Organic Farms (relative to Certified Organic Farms)	Uncertified Organic Farms (relative to Conventional Farms)*	Certified Organic Farms (relative to Conventional Farms)*	Response Count	
Unlikely (0% chance)	6	7	6	9	19.57%
Less likely (25% chance)	7	5	2	10	21.74%
Likely (50% chance)	17	17	19	24	52.17%
More likely (75% chance)	8	4	7	10	21.74%
Absolutely (>75% chance)	7	12	13	13	28.26%

Note: Conventional farms are those that use traditional planting methods involving chemicals and synthetic materials for fertilization, pest and herb control, and other production activities.

Results in table B.3.1 provide interesting results that can be associated with the organic farms' probability of obtaining loans vis-a-vis other types of farmers. For 37.7% of respondents, uncertified organic farms have about 50% chance of obtaining a loan from their institution relative to certified organic farms. This is also the case for uncertified organic farms relative to conventional farms – 37.7% of respondents say that they have 50% chance of obtaining a loan. Meanwhile, 40.43% on the respondents indicate that certified organic farms relative to conventional farms are more likely to obtain loans from their institutions. In general, these results imply that lending institutions' loan decisions are not affected whether an organic farm borrower is certified or not.

B.3.2. Respondents' general perception of organic farm borrowers

Question: *"What is your institution's general perception of organic farm borrowers compared to conventional farm borrowers? Please choose all that apply and ranking your responses as 1 (most prevalent idea), 2 (2nd most prevalent idea), 3 (3rd most) and so on and so forth."*												
	1	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**	**11**	**Rating Average**
Hobby or lifestyle farmers	7	7	9	10	2	1	0	0	0	0	0	**3.27**
Significantly smaller operations than conventional farms	24	8	6	3	1	0	1	0	0	0	0	**3.91**
Health conscious farmers	4	10	9	4	2	1	2	1	2	0	0	**3.18**
Environmentally conscious farmers	5	12	9	5	1	0	1	1	0	1	0	**3.18**
Have too small loan requests (microfinance)	0	2	0	1	4	4	2	3	2	4	0	**2.00**
Fussy farmers – making big deal of trivial stuff	0	1	1	1	0	2	1	0	4	7	6	**2.09**
Sustainable farm businesses	4	2	4	3	4	2	2	5	0	0	0	**2.36**
Stagnant operations with very limited expansion plans	1	0	2	2	0	5	4	5	3	1	0	**2.09**
Less viable farm businesses	1	5	2	1	3	2	3	2	6	1	0	**2.36**
Less optimal business decisions	0	0	3	2	4	3	1	3	2	5	1	**2.18**
Others	0	0	0	0	3	0	2	0	1	1	11	**1.64**

The summary in table B.3.2 provides interesting indications of how lending institutions perceive their organic farm borrowers vis-a-vis conventional farm borrowers. Given a host of pre-conceived ideas suggested by organic farmers in previous focus group discussions, the more prevalent perceptions (except for the "Others" category) that organic farms have too small loan requests (average rating of 2.00), organic farmers are fuzzy (2.09), their operations are stagnant (2.09), and they usually make less optimal business decisions (2.18).