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Report to the Chairman, Subcommittee on Agricultural Credit, Committee on Agriculture, Nutrition, and Forestry, U.S. Senate

May 1993

FARM FINANCE

Number of New Farmers Is Declining

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Resources, Community, and
Economic Development Division

B-251743

May 3, 1993

The Honorable Kent Conrad
Chairman, Subcommittee on
Agricultural Credit
Committee on Agriculture,
Nutrition, and Forestry
United States Senate

Dear Mr. Chairman:

As the average age of the nation's farmers has increased in recent years, Members of Congress have expressed concern over the declining number of new farmers and what the federal government can do to help ease the entry of people into farming. In response to your request, this report provides information on (1) the number of individuals who have started new farming operations in recent years and barriers to their entry; (2) current assistance available to new farmers from the U.S. Department of Agriculture's (USDA) Farmers Home Administration (FmHA) and states; and (3) the implementation status of the beginning farmer provisions in the Food, Agriculture, Conservation, and Trade Act of 1990 (P.L. 101-624, Nov. 28, 1990)—commonly referred to as the 1990 Farm Bill—and in other recent legislation. Additionally, as agreed with your staff, appendix I provides information on lending programs available to beginning farmers in selected, key farming states.

This report summarizes the information that we obtained from USDA's Economic Research Service (ERS), FmHA officials in 20 farm states that were ranked highest in outstanding farm debt and at the agency's headquarters, and state agricultural officials in 12 states that operate beginning farmer programs. Appendix I identifies the 20 states where we contacted FmHA and state officials.

Results in Brief

The number of new farmers has declined considerably in recent years. ERS reported that average annual entry fell about 25 percent during the mid-1980s and federal and state agricultural officials say this decline is continuing. The decline is largely attributable to economic conditions in the agricultural sector that have made farming less financially desirable. Also, those people who are interested in starting to farm face difficult hurdles in obtaining financing to cover the costs of acquiring and operating a farm and in obtaining suitable land to farm.

FmHA, the federal "lender of last resort" for the nation's farm sector, has not targeted loan funds to beginning farmers, but such individuals may obtain loans if they are able to meet the agency's relatively lenient loan-making standards. FmHA has given beginning farmers priority over certain other individuals in leasing or purchasing its inventoried farm properties, but the suitability of these properties for beginning farmers is often questionable. Additionally, some states—12 of the 20 states we contacted—sponsor programs that target loan assistance to beginning farmers. However, beginning farmers may have difficulty in qualifying for credit through these programs or at FmHA.

FmHA has not fully implemented the beginning farmer provisions of the 1990 Farm Bill. As noted earlier, FmHA, in accordance with the act, gave beginning farmers certain preference in obtaining inventoried farm properties. However, it has not implemented other beginning farmer provisions, such as one suggesting that it establish innovative programs for financing and for assisting in land transfers between generations of farmers. To provide further direction to FmHA, in October 1992 the Congress mandated that the agency establish programs targeting farm ownership and farm operating loans to beginning farmers. In February 1993, FmHA was preparing proposed regulations to implement this new legislation.

Fewer People Are Entering Farming

The number of new farmers has declined in recent years. This downward trend is primarily associated with economic conditions in the nation's agricultural sector, the result being that farm occupations have been less financially attractive than nonfarm occupations. Also, demographic factors, such as a declining farm population and birth rate among farm families, have contributed to decreases in the number of farm entrants. Those individuals who are interested in starting farming operations must overcome obstacles in qualifying for credit to cover the costs of acquiring and operating a farm and in obtaining suitable land to farm.

Trend in Farm Entry

ERS analyzed data from the Census of Agriculture to estimate entry into farming during the late 1970s through the mid to late 1980s. In March 1991, ERS estimated that the number of farm entrants—those who began operations on their current farm within a given year of the study period—averaged about 25,000 less on an annual basis during the 1982-87 period compared with the 1978-82 period.[1] Specifically, ERS reported that there were, on average, about 75,000 entrants per year from 1982 through 1987 compared with about 100,000 per year during the previous period. According to ERS, entry declined in all 48 contiguous states, ranging from 9 percent in New Jersey to 48 percent in Wisconsin. Most of the decline in entry—58 percent—occurred among people under 35 years of age. USDA, in commenting on a draft of this report, said that agricultural prosperity during the late 1970s/early 1980s and the agricultural recession during the 1982-87 period need to be recognized in interpreting the results of ERS' new entry analysis. Also, USDA said that entry rates can be affected by unique regional and commodity-specific factors. For example, factors affecting entry into dairy operations in New England are likely to differ from those affecting the growing of potatoes in western states.

Statistics on the number of people entering farming during the late 1980s/early 1990s are not available. ERS plans to report such statistics in 1994, when its analysis of the 1992 Census of Agriculture is completed. However, our work, while not providing national estimates, indicates that the decline in the number of people entering farming has continued into the early 1990s. Specifically, in mid-1992, 16 of 20 FmHA officials in key farm states and 11 of 12 state agricultural officials in states that sponsor beginning farmer programs told us that, over the past 5 years, the number of people entering farming declined by at least 10 percent. For example, both the FmHA Chief of Farmer Programs in Texas and the Assistant Director of Ohio's Department of Agriculture cited declines of more than 50 percent in their states.

Furthermore, a 1990 Iowa State University statewide poll of randomly selected farmers indicated that the vast majority of the 2,288 respondents—85 percent—believe that fewer young people will enter farming in the next 10 years. The results of this poll were reinforced by officials from farm interest groups, such as the Future Farmers of America (FFA), and from commercial farm lenders, such as a Farm Credit System (FCS) bank in Minnesota, who—while unable to provide statistics—told us that interest in starting farming operations continues to decline. For example, FFA's National Executive Secretary said that FFA membership is declining and that the country is approaching a point where many young people in rural areas may not consider farming as a career.

[1]ERS' estimates of the number of farm entrants were based on the most comprehensive data on the subject. These estimates, however, may not be precise because of limitations in the census data. For example, the data (1) included experienced farmers who had changed farms and (2) did not account for farmers who entered and exited between the census periods.

Reasons for the Decline

The general consensus is that recent declines in the number of new farmers are primarily the result of economic conditions in the nation's agricultural sector that make farming less attractive financially. ERS reports in March 1991 and June 1992 stated that the number of farm entrants declined during the 1980s as the severe financial crisis that adversely affected the nation's agricultural sector worsened and potential entrants were swayed to more financially rewarding nonfarm occupations.

Twenty-one of the 32 FmHA and state agricultural officials we interviewed in 20 states told us that the economy is the major factor influencing the decline in the number of people entering farming. For example, the FmHA Chief of Farmer Programs in North Dakota and the Executive Director of Iowa's Agricultural Development Authority told us that the farm economy was the major factor influencing estimated declines of 26 to 50 percent in new farm entrants in their states over the past 5 years. Also, 23 of the FmHA and state agricultural officials we spoke with said that a lack of parental support discourages some farm children from entering farming, and a North Dakota State University professor told us that most farm parents do not encourage their children to enter farming because of its high risks and low profit potential.

University professors in Iowa, North Dakota, and Texas also told us that economic conditions are influencing a continuing decline in individuals' interest in starting farm operations. For example, a Texas A&M University professor told us that prospective farmers are discouraged by farming's low profit potential that limits their capacity to borrow and repay funds, make capital purchases, and accumulate savings. To illustrate, he noted that a livestock operator would require $1 million in operating assets—e.g., land, cattle, and equipment—to generate an annual net taxable farm income of about $40,000, or only about a 4-percent return on investment. Likewise, FFA's National Executive Secretary, as well as FFA representatives in Iowa, North Dakota, and Texas, told us that members' interest in traditional production agriculture is declining as alternative occupations have become more financially attractive. Also, 30 of the 32 FmHA and state agricultural officials we interviewed in 20 states told us that alternative occupational opportunities discourage individuals from entering farming. An Iowa State University professor said today's youth are less willing to endure the personal financial sacrifices necessary to pursue farming when alternative occupations offer greater opportunities.

Additionally, demographic factors may have contributed to decreases in the number of entrants to farming and may have a prolonged effect.

Specifically, entrants to farming have declined, and will likely continue to do so, because the traditional pool of potential new farmers has shrunk. For example, ERS reported in 1991 and in 1992 that decreases in farm entry can be partially attributed to the declining farm population and birth rate among farm families and to improving educational levels among children of farmers, which increases nonfarm employment opportunities.

Obstacles That Farm Entrants Face

The primary obstacles that individuals who desire to enter farming face are income and credit related. For example, according to the 20 FmHA officials we interviewed, the inability of the proposed farming operations to demonstrate sufficient income for debt repayment was the most common reason why beginning farmers were unable to qualify for FmHA loans. Furthermore, officials representing commercial lenders—e.g., three FCS banks, the American Bankers Association (ABA), the Independent Bankers Association of America (IBAA), and seven member banks—told us that funds are available to finance creditworthy applicants, but beginning farmers often do not have the financial resources (equity, projected cash flow, or down payment) or farming experience needed to qualify for loans.

Officials at the Omaha Farm Credit Bank told us that potential beginning farmers generally cannot qualify for FCS credit without financial or operational assistance from relatives or friends. An ABA official said that people new to farming have difficulty because considerable equity is usually necessary to obtain a loan—i.e., some banks will lend a maximum of only 50 percent of collateral value to finance farm operating expenses. An IBAA official added that some banks require a minimum 15-percent cash-flow margin over expenses to demonstrate potential repayment ability on operating loans. The manager of a rural Texas bank told us that beginning farmers usually cannot meet the bank's required 30-percent down payment and lack sufficient equity to offer as loan collateral.

Some beginning farmers also encounter problems in obtaining land that is suitable for independent farming operations. Specifically, in some areas, the restricted availability of farmland may contribute to beginning farmers' inability to lease or purchase property. USDA's Acting Assistant Secretary for Economics said that beginning farmers in areas where commodity programs are prevalent may have difficulty in taking control of farmland because of the higher profit margins available to current program participants. Additionally, the majority of the 32 FmHA and state officials we interviewed said that the limited amount of suitable land for farming may add to the difficulties of those entering farming. For example, the

Executive Director of the Iowa Agricultural Development Authority, as well as a rural banker in that state, said that beginning farmers may have difficulty in purchasing or leasing Iowa farmland because available land is usually sold or leased to established farmers with proven records of successful farming.

USDA, in commenting on a draft of this report, identified other obstacles that beginning farmers may encounter, such as the need to meet environmental regulations, that require special expertise and capital. For example, starting a livestock operation requires meeting animal waste regulations. Also, crop farmers must adhere to new pesticide handling and application rules.

FmHA and State Efforts to Assist New Farmers

While FmHA has not targeted loan funds to beginning farmers, the agency provides opportunities for such individuals to obtain credit through standards that are more lenient than commercial lending standards. Also, 12 of the 20 states we contacted sponsor programs in which financial assistance is targeted to beginning farmers. Nevertheless, beginning farmers may have difficulty in qualifying for the FmHA or state-sponsored loan programs.

FmHA Assistance Available to New Farmers

FmHA does not have a financial assistance program that targets loan funds to beginning farmers. As the lender of last resort for the nation's farmers, FmHA does have relatively lenient loan criteria that apply to all applicants for the agency's loans—e.g., direct loan applicants need only to project income that equals or exceeds their estimated expenses. However, new farmers may experience difficulty in obtaining credit even with FmHA's lenient criteria. Specifically, 14 of the 20 FmHA state office officials said this is a problem for farm operating loans, while 11 said it is a problem for farm ownership loans.

To provide beginning farmers access to farmland, in May 1992 FmHA published regulations in the Federal Register (1) defining a beginning farmer as, among other things, an individual who has operated a farm or ranch for not more than 10 years and (2) giving beginning farmers priority over certain other family farm operators in obtaining the agency's farm inventory properties. However, these actions may do little to stimulate new farm operations because of questions about the availability and appropriateness of FmHA's inventory property for beginning farmers. These questions arise for several reasons.

First, former owners and certain others, such as the previous farm operator of the property, continue to have higher priority in reacquiring farm inventory properties through lease or purchase. Second, FmHA's inventory properties may not be appropriate for beginning farmers (or for other potential purchasers) seeking viable independent farm units for a variety of reasons, such as poor soil conditions, deteriorated farm buildings, or limited acreage. For example, as we reported in April 1991, only 11 of the 72 FmHA farm inventory properties we reviewed in seven states were considered by FmHA officials as appropriate for beginning farmers.[2] As such, many of the agency's properties may be more appropriate as additions to existing operations.

State-Sponsored Programs to Assist New Farmers

Of the 20 key farm states we contacted, 12 sponsor programs targeting beginning farmers. Most of these programs are based on federal tax-exempt bonds issued by states to private lenders, normally commercial banks, who pass on their tax savings in the form of reduced interest rates to the beginning-farmer borrowers. (Authority for the tax-exempt status of these bonds expired in June 1992 and had not been reinstated at the time of our review in February 1993.) Participants in these programs generally have had some farming experience, which may be obtained through leasing farm operations. For example, officials in 10 of the 12 sponsoring states told us that applicants averaged at least 3 years of farming experience at the time of loan approval.

Most of the programs fund the acquisition of farmland and depreciable property—e.g., farm machinery and breeding livestock—but prohibit such purchases from relatives. Few of the programs fund farm operating expenses or debt refinancing. Generally, to participate in these programs, applicants must meet farmland ownership and net worth tests.

As with FmHA's loan programs, beginning farmers face difficult financial hurdles in qualifying for the state-sponsored programs. Specifically, 8 of the 12 state program officials we interviewed said that applicants' inability to meet credit standards is the most common reason for loan denial—e.g., applicants have insufficient projected cash flow to repay debt, have inadequate equity, or are unable to meet down payment requirements. For example, a North Dakota official told us that approximately 30 percent of the applicants in that state's program are denied because they cannot demonstrate debt repayment ability.

[2]Farmers Home Administration: Sales of Farm Inventory Properties (GAO/RCED-91-98, Apr. 9, 1991).

Additionally, in an effort to make land more available to beginning farmers, as of September 1992, 5 of the 20 states that we contacted had recently started programs to assist in farmland sale or lease transfers from owners to beginning farmers. For example, Nebraska started a program in April 1991 that is operated by the Center for Rural Affairs (a nonprofit organization that promotes rural development) and provides a clearinghouse that links land owners, especially retiring farmers, with people who desire to start farming. However, since all but the Nebraska program were initiated in 1992, experience has been limited. Specifically, as of September 30, 1992, Nebraska reported 24 land transfers to beginning farmers, and Iowa reported 1; but Kansas, Minnesota, and North Dakota had not completed any.

Legislative Efforts to Assist Beginning Farmers

The Congress passed two laws in recent years containing provisions that reflect its desire to assist beginning farmers. First, the 1990 Farm Bill includes several such provisions, some of which have not been implemented for various reasons discussed below. Second, more recent legislation, enacted in October 1992, requires FmHA to establish two new loan programs targeting funds to beginning farmers. At the time of our review, FmHA was preparing proposed regulations to implement these new requirements.

FmHA Has Not Fully Implemented the 1990 Farm Bill

FmHA has implemented one of the mandated beginning farmer provisions of the 1990 Farm Bill by giving beginning farmers priority in acquiring its farm inventory property. FmHA has also met another of the act's provisions by defining beginning farmers. However, as of February 1993 FmHA had not yet implemented the other mandated beginning farmer provision, namely, that it establish a market placement program, which would help beginning farmers to locate and secure commercial credit. FmHA officials told us that a similar program is currently available to all potential borrowers and that they plan to issue proposed regulations to establish a program tailored specifically for beginning farmers by the start of fiscal year 1994.

The Congress also used the 1990 Farm Bill to express its sense that FmHA should take three administrative steps to assist beginning farmers: (1) establish innovative programs of finance and assistance for land transfers between generations of farmers, (2) expand the use of the credit sale and land contract method for selling farm inventory property to beginning farmers, and (3) develop statistics on loans made to and inventory farms sold to beginning farmers. However, as of February 1993

FmHA had not undertaken the administrative initiatives suggested by the Congress.

FmHA officials told us they had not established innovative programs of finance and assistance for land transfers because their basic authorizing legislation—the Consolidated Farm and Rural Development Act, as amended (P.L. 87-128, Aug. 8, 1961)—had been silent on whether loan funds could be targeted to beginning farmers. (As discussed later, subsequent to the 1990 Farm Bill, the Congress passed other legislation specifically requiring FmHA to target loan funds to beginning farmers.)

Additionally, FmHA managers told us they have not expanded the use of the credit sale and land contract method for selling farm inventory property because such sales options are already available to all potential purchasers, including beginning farmers. Finally, FmHA officials said they have not modified their computer and finance systems to develop statistics on loans made to and inventory farms sold to beginning farmers because competing demands for computer resources have delayed the work necessary for such modifications. Agency officials estimated that the suggested modifications should be completed by June 1993.

Recent Legislation Requires FmHA to Target Loans to Beginning Farmers

In late 1992, the Congress passed and the President signed the Agricultural Credit Improvement Act of 1992 (P.L. 102-554, Oct. 28, 1992) to, among other things, target FmHA financial assistance to beginning farmers. This act requires FmHA to establish two new loan programs. The first is a farm operating program that targets loan funds to individuals with 5 or fewer years' farming experience. In this program, FmHA assistance is to be available for up to 10 years to borrowers who develop and meet operating plans that provide for their progression to private credit and who agree to participate in loan assessment, borrower training, and financial management programs. This program's aim is to put beginning farmers in a financially viable position, independent of the need for further FmHA financial assistance, within 10 years.

The second is a down payment loan program that targets farm ownership loan funds to individuals with 5 to 10 years' experience in operating a farm or ranch. In this program, FmHA is to provide a 10-year, low-interest rate loan for 30 percent of the farm's value. Program participants are to contribute at least 10 percent of the purchase price as a down payment on the property, and they can finance any remaining portion with another lender. This program's aim is to further enhance the financial viability of new farmers by putting them in a position to build equity in their farming operations.

In February 1993, FmHA was preparing proposed regulations, which agency managers estimated would be issued in April 1993, to implement this recent legislation.

Conclusions

The 1990 Farm Bill and the October 1992 legislation could encourage some people to attempt to enter farming. Also, some features in the new legislation, such as requiring borrower training and increasing FmHA supervision, can potentially help beginning farmers to stay in business. However, a number of important factors might tend to minimize the number of new entrants. These include the impacts of the financial crisis that adversely affected the nation's agricultural sector during the 1980s and the sector's continuing high risk and low-profit potential. Also, even with the existing FmHA and state-sponsored assistance programs, demonstrating the ability to qualify for credit to cover the costs of acquiring and operating a farm and being able to obtain suitable land to farm are difficult hurdles for those who are interested in farming.

Agency Comments

In commenting on a draft of this report, USDA expressed two general concerns. First, USDA said that the draft did not discuss the impact that the changing numbers of farm entrants, as well as changes in the number of people who are exiting farming, may have on various broader policy issues, such as the adequacy of food production, the structure of the nation's farming sector, and the viability of rural economies. While we agree that the policy issues identified by USDA are important, we did not address them in this report because they are beyond the scope of work that you requested.

USDA's second general comment was that the draft did not adequately address the Department's opportunities to provide assistance to beginning farmers as a result of the October 1992 credit act. We disagree with this assessment and would point out that the draft reviewed by USDA (1) described the two beginning farmer programs that are mandated by the act and (2) recognized that FmHA was preparing proposed regulations in February 1993 to implement these requirements.

In addition to these two general concerns, USDA provided a number of other perspectives on issues included in this report, which we incorporated as appropriate. The Department's specific comments and our evaluation are contained in appendix II.

Our objectives, scope, and methodology in conducting this review and preparing this report are discussed in appendix III.

As arranged with your office, we are sending copies of this report to the appropriate Senate and House committees; interested Members of Congress; the Secretary of Agriculture; the Administrator of ERS and the Acting Administrator of FmHA; the Director, Office of Management and Budget; the governors of each state we contacted; and other interested parties. We will also make copies available to others upon request.

Please contact me at (202) 512-5138 if you or your staff have any questions. Major contributors to this report are listed in appendix IV.

Sincerely yours,

John W. Harman
Director, Food and
Agriculture Issues

Contents

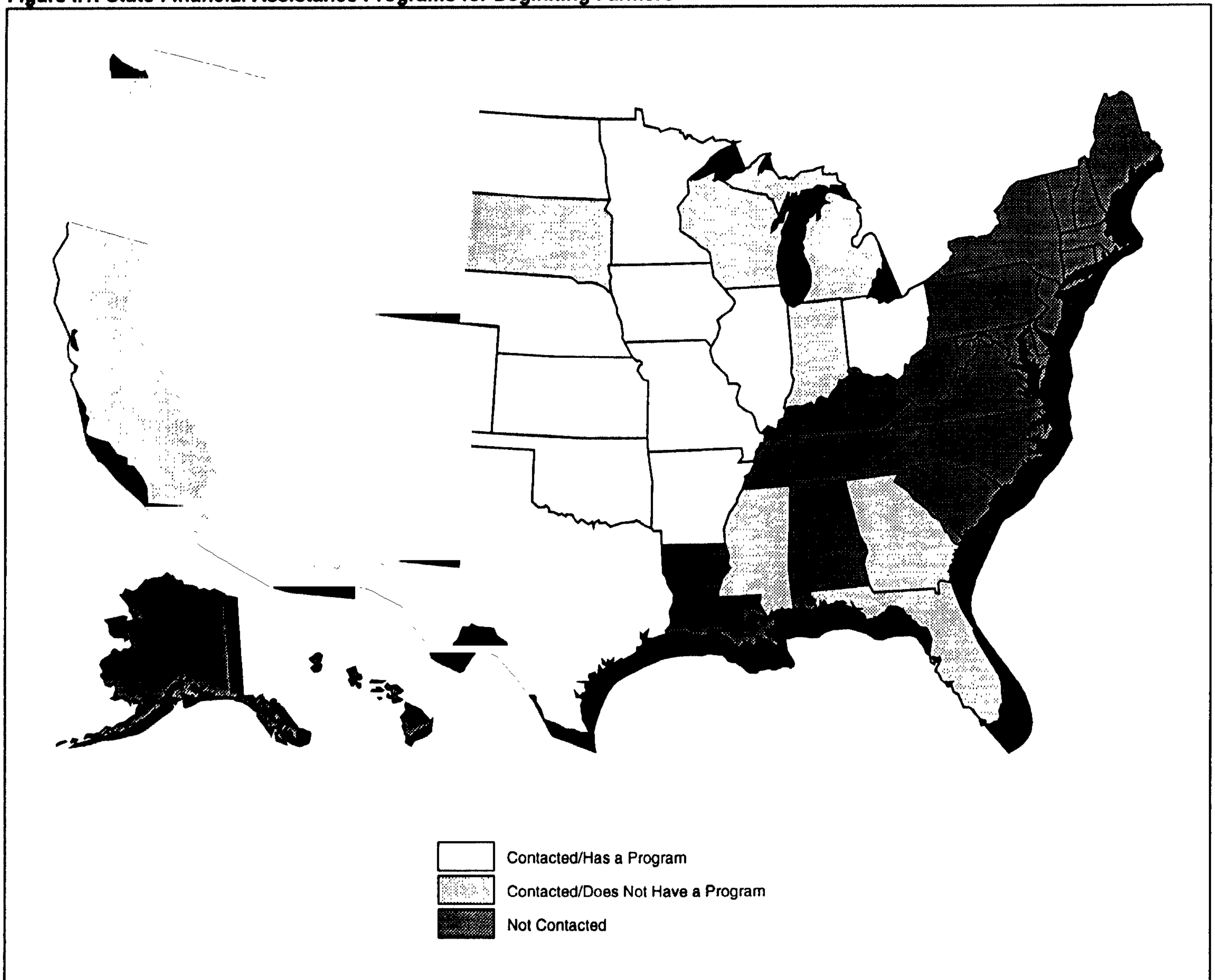
Abbreviations

ABA	American Bankers Association
ERS	Economic Research Service
FCS	Farm Credit System
FFA	Future Farmers of America
FmHA	Farmers Home Administration
GAO	General Accounting Office
IBAA	Independent Bankers Association of America
USDA	U.S. Department of Agriculture

Financial Assistance Programs for Beginning Farmers in Selected States

This appendix provides information on the financial assistance programs for beginning farmers in key farming states. Figure I.1 shows the 20 farming states that we contacted to determine whether they sponsor programs that target financial assistance to beginning farmers; as of June 30, 1992, 12 of these states sponsored such programs and 8 did not. These 20 states were selected because they were the top states in terms of outstanding farm debt. We did not contact the remaining 30 states to determine if they sponsor such programs. (The information in fig. I.1 and tables I.1 and I.2 was provided to us by officials in each state.)

Figure I.1: State Financial Assistance Programs for Beginning Farmers



The programs sponsored by the 12 states vary in age and loan volume. Most impose a $250,000 financing limit and use loan funds generated through the issuance of federal tax-exempt bonds to private lenders, normally commercial banks, who in turn offer reduced interest rate loans to beginning farmers. As such, to participate in these programs, applicants must meet both the states' eligibility criteria and the lenders' credit standards. Table I.1 provides general information on the programs in the 12 sponsoring states.

Table I.1: General Information on Financial Assistance Programs for Beginning Farmers in 12 Key Farm States

Loan values are in dollars in millions

State	Year started	Loan limits	Loan volume through March 31, 1992 Number	Loan volume through March 31, 1992 Value	Funding source
Arkansas	1991	$250,000	1	$ 0.25	Tax-exempt bonds
Colorado	1983	250,000	165	17.80	Tax-exempt bonds
Illinois	1982	250,000	2,026	132.14	Tax-exempt bonds
Iowa	1981	250,000	1,258	106.87	Tax-exempt bonds
Kansas	1990	250,000	173	13.67	Tax-exempt bonds
Minnesota[a]	1987	50,000	251	7.10	State and local lenders
	1989	50,000	15	0.50	State and local lenders
	1991	250,000	12	1.00	Tax-exempt bonds
Missouri	1985	250,000	80	5.20	Tax-exempt bonds
Nebraska	1982	250,000	600	55.00	Tax-exempt bonds
North Dakota	1978	100,000	987	36.72	State-owned bank
Ohio	1985	250,000	28	6.78	Tax-exempt bonds
Oklahoma	1991	250,000	0	0	Tax-exempt bonds
Texas	1992	50,000	0	0	Farm vehicle license plate fees

[a]Minnesota has three separate financial assistance programs.

Similarities exist in the financial assistance programs sponsored by the 12 states. Specifically, most programs have restrictions involving applicants' previous land ownership and maximum net worth. Eligible activities generally include purchasing farmland and depreciable property—e.g., farm machinery and breeding livestock. Ineligible activities generally include paying farm operating expenses—e.g., buying seed or fertilizer—refinancing existing debt, and using program funds for making purchases from relatives. Table I.2 provides information on applicant qualification limits and eligible activities for the programs in the 12 sponsoring states.

Table I.2: Information on Applicant Qualification Limits and Eligible Activities for Financial Assistance Programs for Beginning Farmers in 12 Key Farm States

	Applicant qualification limits		Eligible program activities				
State	**Prior land ownership[a]**	**Maximum net worth**	**Buy farmland**	**Buy depreciable property**	**Pay operating expenses**	**Refinance existing debt**	**Make purchases from relatives**
Arkansas	Yes	No	Yes	Yes	No	No	No
Colorado	Yes	No	Yes	Yes	No	No	No
Illinois	Yes	$250,000	Yes	Yes	No	No	No
Iowa	Yes	200,000	Yes	Yes	No	No	No
Kansas	Yes	No	Yes	Yes	No	No	No
Minnesota							
1987	Yes	206,200	Yes	Yes	No	Yes	Yes
1989	Yes	206,200	Yes	No	No	No	Yes
1991	Yes	200,000	Yes	Yes	No	No	No
Missouri	Yes	150,000	Yes	Yes	No	No	No
Nebraska	Yes	300,000	Yes	Yes	No	No	No
North Dakota	Yes	150,000	Yes	No	No	No	Yes
Ohio	Yes	No	Yes	Yes	No	No	No
Oklahoma	Yes	No	Yes	Yes	No	No	No
Texas	No	No	No	Yes	Yes	Yes	Yes

[a]The limits are less than 15 percent of the median-size farm in the county and a fair market value of no greater than $125,000 for each of the states that have restrictions except for Minnesota's 1987 and 1989 programs, which have a 240-acre limit, and the North Dakota program, which specifies the limit as "less than what the bank considers to be an economic farm unit."

Comments From the U.S. Department of Agriculture

Note: GAO comments supplementing those in the report text appear at the end of this appendix.

DEPARTMENT OF AGRICULTURE
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20250

MAR 1 9 1993

Mr. John W. Harman
Director
Food and Agriculture Issues
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Harman:

Thank you for the opportunity to comment on the draft report entitled Farm Finance: Number of New Farmers Is Declining (GAO/RCED-93-95). The Department is concerned about the problems faced by beginning farmers including concerns that the Department's programs be designed and administered so as to preclude any unnecessary obstacles to individual opportunities for those who wish to enter farming.

Comments from the Economic Research Service (ERS) and the Farmers Home Administration (FmHA) are incorporated in the Department of Agriculture's response. For clarity, comments are organized into the three major discussions of this report: declining number of farm entrants, reasons for the decline, and legislative response.

Declining Number of Farm Entrants

See comment 1.

Although possibly beyond the scope of this report, a discussion of farm entrants within a broader policy context would have been helpful. For example, does the decline in farm entrants pose a threat to the stability and productivity of the nation's food and fiber sector? Could stimulating more entrants into farming reverse the decline experienced by some rural communities? In the latter case, declining farm entrants can more fruitfully be viewed as a rural social policy issue.

To report on declining farm numbers begs the question of how one determines the appropriate number of entrants into agriculture. If viewed from the standpoint of farm production, the entry rate may be sufficient. But, if viewed from the perspective of preserving the current number of farms in the rural heartland, entry rates may be too low. This report fails to address the broad policy context in which declining farm entrants should be evaluated.

See comment 2.

The ERS study cited in this report was one of the first to enumerate farm entrants and exits for a particular period. The data may lead to the wrong conclusions unless it is interpreted within the context of economic conditions that prevailed in the 1977-82 and 1982-87 study periods. In general, these periods represent the peak of an agricultural boom and the trough of an agricultural recession, respectively. The resulting measures of farm entrant declines are useful for examining what happened during these periods of study, as was the authors' intention, but not very useful for extrapolating into the future because a large number of factors influencing

Mr. John W. Harman 2

the agricultural sector have since changed. Also, it would have been useful to note that farm numbers have been in almost constant decline since 1935 and that the rate of decline actually slowed in the 1980's to its lowest rate since the 1940's.

Reasons for the Decline and Obstacles New Entrants Face

See comment 3.

The report largely ignores the fact that regional and commodity specific factors are important to determining entry and exit rates. Factors affecting entry into dairy farming in New England are likely to differ greatly from factors affecting those wishing to grow potatoes in the West. This regional aspect of entry and exit is evident in the ERS report cited, which indicates that although entrance rates fell in all 48 contiguous States, entrance rates were greater than exit rates in 13 States.

See comment 4.
Now on p. 4.

Now on p. 5.

The report concludes on page 5 and elsewhere that "...recent declines in the number of new farmers are primarily the result of economic conditions in the nation's agricultural sector that make farming less attractive financially." Later the report focuses on credit-related aspects as "...the primary obstacles that individuals who desire to enter farming face..." (page 7). Our view is that the prospect of low income is the primary factor explaining the decline in entrants during the 1982-87 period, so we would suggest that the report put more emphasis on the income aspects and less on credit availability.

If sufficient farm income can be generated, then credit should not be a major obstacle to entry. As the report indicates, credit is generally available. The problem facing beginning farmers is that farm income prospects and its variability discourage many from entering farming and those who wish to enter are often unable to generate sufficient income to cover expenses and borrowed capital. Beginning farmers compete with large, better capitalized, and more integrated farms that can operate on smaller profit margins. For some, even the favorable credit terms of FmHA's programs will not overcome deficiencies in income.

The report suggests that credit is pivotal to controlling assets needed to enter farming. It is true that farming is an increasingly capital intensive industry and that low equity beginning farmers, especially, may have difficulty acquiring the necessary capital by using debt financing. But there are ways to acquire the use of assets. For example, leasing is a viable alternative for some, but this frequently used option receives scant attention in the report.

The report tends to treat credit as a generic input. Credit serves a variety of purposes that include the financing of operating expenses, chattel, and farmland. Beginning farmers likely face different needs for and availability of each of these types of credit.

See comment 5.

Other obstacles or barriers to entry are omitted from the report. Increasing environmental, safety, water, and labor regulations are examples.

Mr. John W. Harman 3

Starting a livestock operation means meeting animal waste controlrequirements, while crop farmers must adhere to new pesticide handling and application rules. Meeting these new regulations requires special expertise and capital. Commodity programs also provide obstacles to entry. Programs with acreage allotments are examples. Beginning farmers in areas where these programs are prevalent may have difficulty bidding for control of farm real estate due to higher profit margins available to current program participants.

Legislative Response

See comment 6.

Recognizing the specifics of the Congressional request, the report's focus on FmHA's implementation of the 1990 Farm Bill and its lack of targeting loan funds to beginning farmers does not recognize the program change opportunities offered by the Agricultural Credit Improvement Act of 1992 (P.L. 102-554) which directly addresses beginning farmer issues. The report should clarify that prior to the 1992 Act, FmHA had little authority to target program appropriations to beginning farmers. The Agricultural Credit Improvement Act now gives the agency wide ranging authority to develop regulations to target direct and guarantee loan funds to beginning farmers, and to enter into partnerships with State-run beginning farmer programs.

See comment 7.

The section on State beginning farmer programs should have stressed that these programs are usually very small and some have received little or no appropriations. There are studies that examine the effectiveness of these programs. A 1990 study conducted at North Dakota State University investigated whether participants in that State's beginning farmer program achieved a significantly different level of economic performance than their nonprogram counterparts. The analysis concludes that the program did not improve the performance of program participants. But, the researchers did note the program possessed desirable social attributes such as establishing young people in farming, supporting communities, and developing rural social activities.

See comment 8.

On page 2, the report is subjectively asserting that the suitability of FmHA inventory properties for purchase or lease by beginning farmers is "often questionable." FmHA acknowledges that quality of inventory property for FmHA and other creditors can tend to be marginal. The lower success rate for farmers on less productive farmland helps explain why this type of property comes into inventory more frequently than highly productive farmland. However, beginning farmers are given priority in leasing or purchasing all of FmHA inventory properties, which includes the most desirable properties as well. Additionally, FmHA's inventory tracing system will be modified to measure the number of inventory properties sold to eligible beginning farmers.

In Summary

See comment 1.

The report provides little or no perspective for understanding the implications of declining farm entrants and farm numbers on the broader

See comment 6.

Mr. John W. Harman 4

questions of the adequacy of U.S. food and fiber production, farm structure, or rural economic conditions. In an era of tight Federal budgets, such an understanding is critical to evaluating what the public policy response should be. Also, the report does not adequately address the Department's opportunities subsequent to the passage of the Agricultural Credit Improvement Act of 1992.

Sincerely,

Keith Collins

Keith Collins
Acting Assistant Secretary
for Economics

The following are GAO's comments on the U.S. Department of Agriculture's (USDA) letter dated March 19, 1993.

GAO Comments

1. While we agree that the policy issues identified by USDA are important, they are not discussed in this report because they are beyond the scope of the work that we conducted in response to the Chairman's request.

2. We agree that the results of ERS' study apply only to the changes that occurred during the two study periods and have revised this report to recognize USDA's concerns. Also, the report recognizes that statistics on the number of people entering farming during the late 1980s/early 1990s are not available and that the results of our interviews of FmHA and state officials do not provide national estimates concerning trends in farm entry.

3. We have made revisions to recognize that regional and commodity-specific factors may influence entry into farming.

4. The report recognizes low income as a major reason why people are not attempting to enter farming. Specifically, there is a general consensus that recent declines in the number of new farmers are primarily the result of economic conditions in the nation's agricultural sector that have made farming less attractive financially. Also, we have clarified the report to recognize the relationship of income and credit as primary obstacles to individuals who desire to enter farming.

5. We have revised the report to recognize that environmental regulations may affect the ability of people to start farming operations and that beginning farmers in areas where commodity programs are present may have difficulty obtaining farmland.

6. We disagree with USDA's assessment regarding the potential for program changes as a result of the Agricultural Credit Improvement Act of 1992. The report describes the two beginning farmer programs that are mandated by the 1992 act and recognizes that FmHA was preparing proposed regulations in February 1993 to implement these requirements.

7. Appendix I provides information on the number and value of loans made, as well as the funding sources, in the state programs for which we compiled data.

8. USDA acknowledged that the productivity of farm properties that enter FmHA's and other creditors' inventories tends to be marginal. It is because of the marginal nature of such properties that we raise a question about their appropriateness for beginning farmers. Also, USDA stated that beginning farmers are given priority in leasing or purchasing all of FmHA's inventory properties, including the agency's more productive ones. USDA's comments failed to recognize that certain others, such as former owners, have a higher priority than beginning farmers in acquiring FmHA's farm inventory properties.

Objectives, Scope, and Methodology

On November 14, 1991, the Chairman, Subcommittee on Agricultural Credit, Senate Committee on Agriculture, Nutrition, and Forestry, requested that we gather information on the entry of people into the nation's farming sector and on FmHA's implementation of the 1990 Farm Bill's beginning farmer provisions. On the basis of the Chairman's request, we focused our work on

- the number of individuals who have started new farming operations in recent years and barriers to their entry,
- current assistance available to new farmers from FmHA and states, and
- the implementation status of the beginning farmer provisions in the 1990 Farm Bill and in other recent legislation.

Additionally, as agreed with the Subcommittee's staff, we compiled information on financial assistance programs that are available to individuals who have expressed an interest in starting farming operations in selected, key farming states.

To gather information on the number of people who have started farming in recent years and to determine the barriers that hinder or prevent their entry into the industry, we reviewed, among other things, reports by ERS and publications from major universities, such as Iowa State University, North Dakota State University, and Texas A&M University. Also, we interviewed representatives of FmHA, officials from states that sponsor programs that target financial assistance to beginning farmers, officials from commercial lending organizations, university professors, and farm interest groups.

Specifically, we used ERS reports for national data on the number of people who have started farming and for information about why the number of new farmers has declined in recent years. Additionally, we focused attention on 20 key farming states to compile specific information about new farmers and why people are or are not entering the industry. These 20 states are those identified in figure I.1 in appendix I as having or not having beginning farmer assistance programs. We selected these states because they were the top 20 states in terms of outstanding farm debt in recent years.

FmHA's input was primarily obtained through the use of a structured interview that we administered to the Chief(s) of Farmer Programs in 20 of the agency's 46 state offices. Interview questions covered such topics as whether there had been a decline in the number of persons entering farming in the past 5 years in those 20 states and, if so, what factors influenced the decline. We administered these interviews by telephone with FmHA state officials in 17 states and by visits with officials in Iowa, North Dakota, and Texas. Also, we interviewed FmHA national office officials to obtain their views on the decline in new farmers in recent years.

We used a second structured interview, which paralleled the one we used with FmHA officials, to obtain information and views from state officials. Specifically, state agricultural officials in 12 of the 20 states that sponsor financial assistance programs for beginning farmers were asked questions such as what factors have discouraged people from entering farming. We administered these interviews by telephone with officials in nine states and by visits with officials in Iowa, North Dakota, and Texas.

We also interviewed commercial lenders to obtain their views on the reasons why people are not entering farming. Specifically, we interviewed officials representing the national Farm Credit Council and the Farm Credit System's Farm Credit Banks in St. Paul, Minnesota; Omaha, Nebraska; and Austin, Texas. Also, we interviewed American Bankers Association and Independent Bankers Association of America officials in Washington, D.C., and officials at seven agricultural banks that we judgmentally selected in Iowa, North Dakota, and Texas. We asked these officials to provide their views on whether interest in starting new farm operations is declining and, if so, why.

We obtained information from the academic community by interviewing professors at three universities—Iowa State University, North Dakota State University, and Texas A&M University. We selected these individuals because they have written extensively on agricultural issues. We discussed the professors' opinions on issues related to beginning farmers, such as the reasons why interest in starting to farm has declined and the problems that new entrants face, such as acquiring operating capital and land to farm. Additionally, we interviewed officials of farm interest groups, such as the Future Farmers of America, Center for Rural Affairs, National Farmers Union, and National Family Farm Coalition, to obtain their views on interest in starting farming and problems that beginning farmers face.

To determine FmHA's efforts to assist new farmers, we reviewed FmHA's internal documentation and interviewed officials at the agency's Office of Farmer Programs in Washington, D.C. We discussed with these officials the agency's loan programs and the criteria that applicants, including beginning farmers, must meet to obtain loans. Also, we reviewed FmHA's proposed regulations published in the May 29, 1991, Federal Register, and interim regulations published in the May 7, 1992, Federal Register, granting beginning farmers priority over certain other operators of family farms in acquiring the agency's farm inventory properties. We also used our interviews of officials in FmHA's Office of Farmer Programs to gather information on the agency's actions to implement the other beginning farmer provisions of the 1990 Farm Bill. Specifically, we discussed with the agency's managers each provision of the bill and what actions the agency had taken, as of February 1993, on those provisions.

To determine state efforts to assist beginning farmers, we contacted agricultural officials in 20 key farm states to determine whether their states sponsored such programs as of June 30, 1992. We obtained from officials in each of the 12 states that sponsor programs (1) descriptive documentation including funding sources and participation criteria and (2) statistical data covering, among other things, the number and value of loans made from inception through March 31, 1992. The information we obtained from these officials is the basis for the tables covering state-sponsored programs in appendix I. We also contacted the National Council of State Agricultural Finance Programs to add assurance that we had not overlooked beginning farmer programs in the eight states where the state officials told us there were none.

During 1991 and 1992, we testified twice at congressional hearings on beginning farmer proposals. First, shortly before the Chairman's request, we testified before the Subcommittee on Conservation, Credit, and Rural Development, House Committee on Agriculture, on FmHA's assistance to individuals who want to start farming operations.[1] That testimony was based on two reports we issued that have implications for beginning farmers.[2] Second, during the course of our review, we testified before the Subcommittee on Conservation, Credit, and Rural Development, House Committee on Agriculture, on, among other things, H.R. 4906—the proposed Agricultural Credit Improvement Act of 1992, which called for establishing programs to aid beginning farmers.[3] The proposed act, as

[1]For a transcript, see Farmers Home Administration: Farmer Program Assistance to Beginning Farmers (GAO/T-RCED-92-4, Oct. 8, 1991).

[2]Farmers Home Administration: Use of Loan Funds by Farmer Program Borrowers (GAO/RCED-90-95BR, Feb. 8, 1990) and Farmers Home Administration: Sales of Farm Inventory Properties (GAO/RCED-91-98, Apr. 9, 1991).

[3]For a transcript, see Farmers Home Administration: Farm Loan Programs and Proposed Changes (GAO/T-RCED-92-59, Apr. 29, 1992).

amended, subsequently passed the Congress and was signed by the President in October 1992 (P.L. 102-554, Oct. 28, 1992). To provide information in this report on recent congressional efforts to help beginning farmers, we reviewed the legislative history of this act and analyzed its beginning farmer requirements. Also, we interviewed FmHA's managers in the Office of Farmer Programs to determine their plans for implementing the beginning farmer provisions of this recent legislation.

We conducted our review from November 1991 through February 1993 in accordance with generally accepted government auditing standards.

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