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How Big Is Nontraditional Finance?

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A diverse group of lenders provides credit to U.S. agriculture outside traditional farm lending relationships. As discussed in the first article in our series, nontraditional finance can be a categorized into three groups: high-volume, branchless lenders; vendor finance; and collateral-based lending. In this article, we provide a range of feasible debt levels held by each group.

Before we begin this exercise, it is important to emphasize that we *cannot* provide an exact estimate since many nontraditional lenders are not subject to public reporting of loan volume. The Economic Research Service forecasts that 2019 total farm sector debt was $415.5 billion. Several categories are based on regulatory reports, including Farm Credit System loans, Farmer Mac, Farm Service Agency, commercial banks, and life insurance companies. For sources without public reporting, ERS estimates rely on ARMS responses. While we estimate lending volume under the three main categories of nontraditional finance defined in our first article, we do not account for credit card debt, loans between individuals, etc. Accounting for nontraditional finance in USDA farm sector debt estimates is an important topic for future research that is far beyond the scope of this article. The purpose of this article is to estimate the potential magnitude of nontraditional finance relative to total farm debt, while drawing attention to the implications of limited data.

High-Volume, Branchless Lenders

ERS estimates that life insurance companies had a loan volume of $15.9 billion in 2018, which was 4% of total farm lending. MetLife recently reported a $20 billion portfolio of farm loans that, along with that of other insurance companies, might lead to larger estimates of agriculture lending; however, some of these loans would not be for production agriculture, for example, timber or nonfarm agribusiness lending. Rabo AgriFinance recently reported a $15 billion farm loan portfolio, which is equivalent to about 3.6% of 2019 farm debt. Volume from nonbank lenders not subject to reporting loan volume likely makes lending from this category higher than combined ERS estimates of life insurance companies and Rabo AgriFinance-estimated loan volume. Thus, we conclude that these lenders made up about 8 percent to 10 percent of all U.S. farm lending in 2019.

Vendor Finance

John Deere Financial is the main lender in this category subject to regular reporting. It had $2.4 billion total farm loan volume in 2019, which would be about 0.6% of all farm loans. Many input suppliers provide vendor credit through both John Deere Financial and Rabo AgriFinance, as well as several internal suppliers, as previously reported. We speculate that although Rabo's vendor finance volume may be lower than Deere's, together they could make up about 1 percent of all farm lending. The Economic Research Service estimates that the 2018 balance of accounts payable on all farms was about $8.2 billion, or $4,087 per farm, but (1) a large share is likely not overdue and (2) vendor finance should technically be reported as short- term debt. Assuming that 3 percent is overdue and "effective credit," which was on the moderate to high end of delinquencies for many commercial banks in 2018, we would have nearly $250 million of additional debt, which is a very small share of total farm sector debt. The volume of debt from Nutrien Finance, CNH Industrial Capital and other players in this category is unknown, but we have no reason to believe it is jointly larger than Deere's and Rabo AgriFinance's combined. Based on these estimates, we believe a conservative estimate of vendor finance is 1.5 percent to 2.5 percent of all farm debt.

Collateral-Based Lenders

Collateral-based lenders do not face regulatory reporting and encompass several relatively new lenders. Some agricultural economists have estimated that these groups hold 2 percent of total farm debt. Educated guesses are the best anyone can do in this category, given the lack of data. We have no evidence or reason to believe that this category of lending is larger than more well-established vendor finance, so are most comfortable with an estimate in the 1-percent-to-2-percent range.

Total Nontraditional Finance

We have defined nontraditional lenders as institutions that offer credit outside a local branch/local officer model and are reasonably confident that these types of lenders hold at least 10 percent of all farm debt. The number could be as high as 15 percent, but stronger claims would require much better data on nonbank or private lenders. Further, there is some uncertainty regarding the numerator and denominator when estimating nontraditional finance as a share of farm debt. In other words, if we are not confident of our estimates of nontraditional finance, then we don't know total farm sector debt.

Implications for Farm Debt at Risk

This analysis prompts the question, Is 10 percent to 15 percent a "large" or "concerning" number? Certainly, the majority of nontraditional credit, especially that held by high-volume, branchless lenders, wouldn't be considered particularly risky. On the other hand, vendor credit or collateral-based lending is often reported to be used by financially stressed farms. Suppose that 10 percent of nontraditional finance (largely vendor credit and collateral-based lending categories), or 1 percent of all farm debt, is held by financially stressed farms that would otherwise be delinquent with traditional lenders. Most commercial banks and Farm Credit System lenders today report delinquencies equivalent to 1 percent to 3 percent of total lending volume. Thus "unobserved" farm debt could hypothetically mean that farm debt at risk is *double* what is reported by commercial banks and Farm Credit lenders. This may be a wild *over*estimate; the point here is that *we don't know,* and it is easy to show that an official measure of farm financial stress may be substantially underestimated. In the next article, we report the results of a novel, in-depth study of vendor credit by feed manufacturers in the Northeast, through which we are able to link the use of vendor finance to farm financial status.

We welcome feedback and questions sent to jifft@cornell.edu.

Reference

Fiechter, C. and J. Ifft. "What Makes Nontraditional Finance Nontraditional?" *farmdoc daily* (10):50, Department of Agricultural and Consumer Economics, University of Illinois at Urbana-Champaign, March 18, 2020.