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Trends And Projections In United States Agriculture With An Alternative Approach For The Financing Of Small Family Farms

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"TRENDS AND PROJECTIONS IN UNITED STATES AGRICULTURE WITH AN ALTERNATIVE APPROACH FOR THE FINANCING OF SMALL FAMILY FARMS"

by

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A thesis submitted to the Department of Business Administration and Economics of Carroll College in partial fulfillment of the requirement for academic honors with a Bachelor of Arts Degree in General Business and Finance

Helena, Montana

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This thesis for honors recognition has been approved for the Department of Business Administration and Economics.

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TABLE OF CONTENTS

PREFACE 1

INTRODUCTION 2

CHAPTER I: HISTORY AND POPULATION EFFECTS
  Introduction 5
  History of Famine 6
  Impacts of Population 10
  First Conclusion 16

CHAPTER II: TRENDS IN U.S. AGRICULTURE
  Introduction 17
  Trends:
    Farm Population 19
    Number of Farm Units 23
    Farm Production 25
    Farm Real Estate Values 29
    Farm Income 32
    Energy Costs 36
  Second Conclusion 40

CHAPTER III: PROPOSED REVISIONS TO THE FARMERS HOME ADMINISTRATION
  Introduction 41
  Debt Financing Sources 44
  Recommended Changes to FmHA:
    Purpose and Lending Criteria 52
<table>
<thead>
<tr>
<th>Topics</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Organization</td>
<td>54</td>
</tr>
<tr>
<td>Revised Definition of Small Farm</td>
<td>56</td>
</tr>
<tr>
<td>Interest</td>
<td>58</td>
</tr>
<tr>
<td>Land Use Policies</td>
<td>60</td>
</tr>
<tr>
<td>Third Conclusion</td>
<td>63</td>
</tr>
<tr>
<td>FINAL CONCLUSION</td>
<td>64</td>
</tr>
<tr>
<td>NOTES</td>
<td>66</td>
</tr>
<tr>
<td>BIBLIOGRAPHY</td>
<td>70</td>
</tr>
</tbody>
</table>
LIST OF FIGURES

Figure #1  WORLD PRODUCTION  11
Figure #2  U.S. POPULATION & FOOD CONSUMPTION  14
Figure #3  FARM POPULATION  20
Figure #4  PEOPLE EMPLOYED ON FARMS  22
Figure #5  U.S. CROP & LIVESTOCK PRODUCTION  26
Figure #6  U.S. FARM PRODUCTIVITY  28
Figure #7  CHANGE IN FARM REAL ESTATE VALUES  30
Figure #8  NET FARM INCOME  34
Figure #9  INCOME FROM FARMING  35
Figure #10  ENERGY PRICES PAID BY FARMERS  37
Figure #11  WHO HOLDS FARM DEBT  50
         (REAL ESTATE)
Figure #12  WHO HOLDS FARM DEBT  51
         (NON REAL ESTATE)
PREFACE

The specific purpose of this thesis is to propose revisions to the purpose and mission of the Farmers Home Administration as it exists today. The need for such modification is suggested by a review of the past history of agriculture and the agricultural trends now being established in the United States. It is specifically the emergence of a return to small farming units which dictates that such action is necessary to sustain the movement and its resultant benefits.

Because this new direction has not had sufficient time to develop a significant statistical history, it is necessary to synthesize to a degree some of the data in order to develop a proper model. Due to the dearth of research material, the related discussion will have to be considered as a set of hypotheses to be further monitored, discussed, criticized, revised and researched.
INTRODUCTION

"Ill fares the land, to hastening ills a prey,
Where wealth accumulates, and men decay,
Princes and lords may flourish, or may fade;
A breath can make them, as a breath had made.
But a bold peasantry, their country's pride,
Once destroyed, can never be supplied."  

Oliver Goldsmith 1772

"City people have forgotten agriculture, and
they had better realize that no civilization
has survived without it. They need to under-
stand it, to be benevolent toward it, because
they need it. No country becomes strong with-
out it, or remains strong without it. Apparently
when you are too successful in society you turn
around and destroy it."  

Emil M. Mrak 1972

Mr. Mrak's statement as Chancellor Emeritus of the
University of California at Davis in May of 1972 appears
to repeat, or to interpret in modern English, the poetic
declaration made some two hundred years earlier by the
Irish journalist and poet, Mr. Oliver Goldsmith. If we
should elect to accept the content of either quotation as a prediction of the events to come, it could be stated that both of these gentlemen possessed the true powers of prognostication.

This country, if not the entire globe, has been experiencing a rapidly accelerating decline in the total farm population with a trend being established which could eventually replace the small family farm units with the giant corporate farm structure. This trend forces the small farmer to seek gainful employment in the suburban areas. Our present day society now appears more devoted to the development of high technology in such diverse fields as space exploration, computerization and communications than with the concentrated effort to strengthen the basis of all survival which is the ability of the country to produce adequate foodstuff to sustain life. Our younger generations are being taught that food and fiber have origin on the shelves of the local supermarkets. Our planners and the developers are continuing to exploit the fertile soils of our country to develop housing and shelter for the mass of population now scurrying to the city environment in search of employment. Concrete has laid the soils to permanent rest and destroyed acres upon acres of productive and potentially productive lands. Mr. Mrak must have obviously concluded that our society has indeed become too successful and the process of planned destruction of our national strength through ignorance of the importance of agriculture has been activated.
"History often repeats itself" is more than just an often repeated adage which Mr. Mrak must have seriously reflected upon when he charged us to be responsible and benevolent towards agriculture.

Farming in the United States is constantly undergoing dramatic changes. These changes are reflected in the many headline topics such as: farm corporations, re-evaluation of farm properties for tax purposes, tractorcades, foreign land ownership, subsidies and embargoes. These mirror the constant evolution in farming. The statistical data now being accumulated and correlated by the United States government and bureaus of various agribusiness related entities is beginning to reflect a slight change in the trends which have prevailed during the past two centuries.
CHAPTER I

HISTORY AND POPULATION EFFECTS
INTRODUCTION

In order to comprehend the importance of maintaining a strong and viable agricultural economy it is beneficial to review and understand the reactions of prior generations to conditions of the past. This may give us insight as to how various factors impacted upon their decisions. We know that agriculture is truly the finest example of the theory of supply and demand economics.

The growing forces of population create a natural demand for commodities produced by farmers. Provided that we are able to understand the relationship of history with the projections of the future, this country can stabilize the farm economy to avoid the errors of the past.

This section reviews that history of farming and the expected growth of a demanding population.
HISTORY OF FAMINE

The study of ancient, medieval and modern history develop solid evidence of society having suffered the ravages of famine. Close scrutiny shows a broad band of causes including, but not limited to, draught, flood, pestilence, human greed and a total lack of understanding of the economics of agriculture. Modern day economists and prophets now challenge us to be aware of a new omen, the real possibility of famine caused by the inability of all agriculture activity to produce massive food supplies which will be demanded by the rapid acceleration of the world's population. The total premise of agriculture today, whether observed on a regional, national or international basis, is to produce sufficient foodstuff and fiber to feed, clothe and shelter that population. While we in the United States have enjoyed a true measure of agricultural success, the greater portion of the world has experienced a very real and continuing series of production failures.

History does in fact make reference to famine as early as 3500 B.C. in Egypt. Chronicles of the time reveal that the Nile River failed to overflow its bank and deposit the annual moistures and nutrients. Food supplies grew so severe that cannibalism became widespread throughout the empire.
A famine which ravaged the Roman Empire had equally hedious results and persisted for some twenty years. It is interesting to note that the pattern which developed the food shortage can be closely compared to Mr. Mrak's quotation. The Romans were devoted agriculturists. They were knowledgeable in the fields of botany, irrigation, fertilization and cultivation. As the population became more sophisticated the distribution of wealth allowed for the growth of larger land holdings devoted to the production of crops which produced the greatest monetary value. This eventually led to the development of farming which specialized in olives and grapes with a total disregard for the production of basic foodstuff such as grains and vegetables. The Romans became careless about domestic agriculture and chronic starvation persisted among the lower classes. Small farms were abandoned in favor of city employment. The government, fearing rebellion by the masses, decreed a dole of bread was the hereditary right of all of the people. This was perhaps the beginning of 'bread politics'. A similarity can be observed by comparison of the trend in social welfare programs we see in the United States today. The Roman government countered this movement from the farm to the city by declaring the provincial governments were to produce their own supply of grain and other food supplies. The insistence upon this policy format eventually led to the downfall and eventual destruction of the empire.

In the late eighth century France experienced the
worst major food disaster in Europe. Grain crops were besieged with a fungus called "Ergot" which rendered a large percentage of grains totally unacceptable for human or livestock consumption. The infestation of cereal grains was so toxic as to cause seizure and eventual death. The impact of the infestation caused famine to prevail throughout the continent and historians note that the results were in evidence until the fourteenth century. The population which survived the onslaught did so on diets of herb soups and native fruits and were sometimes forced to resort to eating tree bark.  

As late as 1700, history records that the population of France was starving to death as the famine persisted. Within fifteen years nearly one-third of the population had died of starvation.  

Britain suffered over two hundred famines from the tenth to the mid-eighteenth century. Food growing gave way to sheep grazing and displaced the small English landholders who migrated to the industrial slums where diet was less substantial than on their own farms. A similar trend is easily recognized by the study of demographics in the United States during the past four decades.  

The Irish potato famine, which occurred roughly 135 years ago, had the severest national impact of any recorded famine and actually altered the demographics and the politics of the United States. This was probably the first instance of a mono-cultured society. As a result
of blight damaged harvests, food supply became so depressed that an estimated one million, or twelve percent, of the Irish population was decimated by starvation.  

The evidence persists that the countries of the Far East were once highly developed agriculturally oriented societies and experienced the trend to larger and larger farming operations, and perhaps sustained the decline of production of edible foodstuff by attempting to develop highly tradeable crops. It is only necessary to observe the continued famine in such countries as India and Pakistan where development of atomic power plants and bombs are under development while attention to feeding the masses is totally ignored to draw a parallel with the prior quotations of Goldsmith and Mrak.

With the world population continuing on the rise, we should become acutely aware of a new cause of potential problems. We may have in effect a revolution of rising expectations superimposed on a population explosion, while living in a world with fixed dimensions and limited capacity to produce.

The review of American agricultural history would lead one to conclude our productive capacity does have its limitations, which are just now becoming evident. It would also lead to the conclusion that for the past several decades our progress may have been more properly directed, and that agricultural development does not necessarily prevent nor preclude famine.
IMPACTS OF POPULATIONS

The plague of population growth on a world wide basis is now beginning to impact upon the nations which have to some degree controlled population growth while continuing to maintain or develop additional capacities to produce adequate food commodities for human consumption in amount sufficient for survival. Demands are now being made upon any surplus production to feed the masses in countries without the production capability. It also appears that there is a parallel between nations whose population growth continues unchecked, in that those countries are experiencing a decline in production ability to support that growth. In 1798 Robert Malthus produced his famous "Essay on Population" in which he concluded that the population, when unchecked, will increase in geometrical ratio while its subsistence will increase in a purely arithmetical ratio. Malthus further asserted as a fact that population always increases up to the limits of the means of subsistence.

The graph titled World Production (figure #1) details the actual production of foodstuff by using the year 1965 as a basis equal to 100 percent. This shows that the food production on a world wide basis had increased by 40 percent by the year 1980.
Figure #1: WORLD PRODUCTION

Source: USDA Handbook of Agricultural Charts
If one graphically displays the world population growth beginning in 1965 through 1980 it becomes obvious that the 1965 population of 3.275 billion has increased at a compounding rate of nearly 3 percent to reach the 1980 estimates of 4.492 billion. If it can be presumed that the world food production was consumed in total by the 1965 population, a graphic comparison of population to food production reveals that population is out-growing its ability to provide sufficient foodstuff. Although this may present an unfair position if the 1965 food consumption level was not in fact 100 percent, it clearly indicates that regardless of the assumed percentage of consumption in 1965, as time passes, so will the demand exceed the supply. This clearly and dramatically indicates the theory of the Malthus essay. Malthus, in 1798, could not have preceived the availability of agriculturally productive farm lands in the United States or the technical advancements in equipment. Consequently his thesis may be more applicable today than it was when originally presented.

If the proposition is correct that 1965 represents the year of complete consumption of food sources, and the graph discussed accurately reflects world growth, the end result will require production increases of food supplies of nearly 30 percent during the next five years to supply adequate production for a minimum survival level in 1985. One must note that the mechanical and technical
revolutions experienced within the United States over the past century have not produced agricultural production increases of the magnitude now required to meet the need of the world's expanding masses. This is revealed by a review of figure #1.

Statistically the United States is not experiencing a full three percent annual population increase as are the majority of underdeveloped countries and the newly developing third world governments. The graph titled United States Population and Food Production (figure #2) provides the same information as figure #1, except it shows that United States farms do provide adequate food supplies. A population growing at a slower rate permits development of surplus commodities with consumption per capita decreasing slowly. Modern morality demands that highly developed agri-societies share the excess with the less fortunate; therefore, when we discuss the demands of population, the representation made by figure #1 may be more realistic than figure #2 which may be conservative.

Although statistics are not available to illustrate or to document we do have the chronicled history of prior great empires to show with clarity that as population increases, the distribution of that population shows movement from farming to non-farming endeavors. The historical section of this report outlines that trend during the period of Roman greatness. The decrease in the number of farms in the United States can be traced from the original
Figure #2: U.S. POPULATION AND FOOD PRODUCTION

Source: USDA Handbook of Agricultural Charts
census conducted in 1790. That census revealed that of the four million inhabitants, nineteen of every twenty were rural dwellers and generally accepted to be farmers. In the 1820 census 93 percent of the population was designated as rural and 73 percent engaged in actual farming practices. By 1870 the number of people actually engaged in raising crops or livestock had dwindled to 53 percent. The 1920 census was the first to indicate that less than one half of the population could be classed as rural dwellers and not more than 25 percent were gainfully employed, or actually earning a living from the production of food and fiber. The 1980 census reveals the figure to be actually approaching three percent of the entire population.
Reviews of history and cultures as they relate to the ability to provide basic necessities of survival, coupled with an inspection of the distribution of population in society, do lead to the conclusion that history has indeed repeated itself. As Goldsmith and Mrak noted, a moment of unconcern in the passing of time may lead to a disastrous and catastrophic reduction in the world's food production.

For perhaps the first time in the recorded history of farming in the United States, recognition of historical events now combined with the economics of energy and inflation are about to create an atmosphere which will dictate certain changes in the patterns of farming in this country and perhaps the world.

These changes should generate a continuing series of new opportunities. Each of these new opportunities will create a new and perplexing series of challenges which must be met if this country is to continue in its place of prominence in the field of agriculture and if it is to retain a sound economy through a proper balance of trade.
CHAPTER II

TRENDS IN U.S. AGRICULTURE
INTRODUCTION

Farm structure has historically been a major force in American history. Farm structure, simply stated, is the control and organization of resources needed for farm production. Its dimensions include the number and the size of those farming units, the capacity of each unit to produce food or fiber, the relationship of inputs to production results, the ownership of lands, the barriers of entry and the final ability to produce incomes and profits.

The structure of American farming has always encountered forces and changes, but apparently never more dramatically than in the past decade. Although we as a nation rely heavily on historical representations to predict future events, the sudden shift in pattern within the industry of agriculture caught us unaware and perhaps slightly unprepared for the change in structure we are continuing to experience.

These new trends and forces will continue to exert their influences on the structure of the American farm system. The end result now appears to be the reversal of the trend to large corporate farms, and the injection of new farming units in the forms of smaller family farms.

This section will attempt to define historical trends, establish the change and project the future effects on the
farming structure of this country.

Graphic displays as well as short narratives, both allowing for future possibilities and probabilities, are to be used to solidify the conclusion surrounding the current reversals. Farm population, employment, number and size of farm units are used in portraying the present reversal of trends. Also included are various other significant trends within the agriculture business that will provide the incentive for continuation of the new changes.
FARM POPULATION

The farm population trend in the United States has continued to decline in aggregate numbers as well as in percentages during the period from 1935 to 1977. The graph on Farm Population in the United States (figure #3) charts the trend. In 1978 a slight reversal in the continuing decline was noted, and the 1979 population remained above the low of 1977. The census for 1980 indicated again a slight growth in farm population. The graph of population is predicated upon a specific definition of the population it graphically depicts. It would appear that the United States Department of Agriculture made an attempt to retain the graphic decline by changing the definition. The original definition was; those living on places of ten or more acres with $50.00 in sales and under ten acres with $250.00 of sales. Utilizing this definition the increase is obvious. The new definition includes those living on places with $1000.00 or more in agricultural sales. The effect of the newest definition permitted the decrease to continue, at least through 1978. The latest information now available and published in the Wall Street Journal's series on agriculture, quotes the U.S. Department of Agriculture as recognizing an increase in rural population. The new definition would have continued to show a decline, if in fact there was no change in population. The admission by the U.S. Department of Agriculture proves that sufficient numbers of people have
Figure #3: FARM POPULATION

Source: USDA Handbook of Agricultural Charts
moved into farming to offset the intent of the definition. The U.S. Department of Agriculture also is reporting a significant change in the number of American farms.22

Regardless of the definition of small farms, one may logically conclude, based upon information being disseminated by that governmental agency, that the trend having origin in 1935 has been altered. It is only a matter of degree of increase, depending upon the definition we wish to accept.

Further proof of the ending of the decline may be observed in the graph depicting the number of people employed on farms (figure #4). According to government statistics nearly 100,000 more workers were employed in 1980 than in 1979, bringing the total to 3.9 million people.23 It is also interesting to note that the distribution in 1979 indicates that 2.5 million were classed as family workers and 1.3 million classed as hired workers. In 1980 those numbers had changed to 2.7 million and 1.2 million respectively.24 This would appear to justify the conclusion that more individuals are now engaged in family farm units.

As to the root cause for the reverse migration, government officials and agri-business editors are speculating that a combination of high food costs, crime levels, and general inflation have encouraged the return to small family farm units. As one editor stated, "For now, it may be enough to settle for a guess that, for many citizens, life in the U.S. cities hasn't been all that rewarding."25
Figure #4: PEOPLE EMPLOYED ON FARMS

Source: USDA Handbook of Agricultural Charts
Projections of the U.S. Department of Agriculture on both figure #3 and figure #4 indicate the likelihood for continued growth in these new trends. Farm population (figure #3) shows the expected increases will reach 9 million by the year 1985, a point unequalled since 1975 when sustained decreases forced it to this level. The year 1985 should also see a slight continued increase in the number of family workers (figure #4). The total of farm workers should then stabilize as the number of hired workers begins a negative cycle. This decrease may possibly result from increased mechanical efficiency on the large farms and a more labor intensive trend by family members on the family small farms.

NUMBER OF FARM UNITS

The number of farm operators has been declining since the peak of 6,812,000 in 1935. This trend continued but the decline in the more recent years did not appear to be as precipitous as in earlier years. In fact, a dramatic change evolved over the past five years. The actual number of farm operations increased. The government still remains saddled with statistical data from the last farm census in 1974 and inputs that information to project future trends. The projections made utilizing the 1974 input included processes of extrapolation of trends, negative exponential functions, Markov process and age cohort analysis. The 1974 information is still a factor
in the information being disseminated in 1980. However, as the new material and information is collected from the 1980 census the evidence points toward a movement away from the credibility of earlier projections. Several of the most recent publications of the Department of Agriculture acknowledge that functional operations of departments will have to change because of the growth of small farms. The Fact Book on U.S. Agriculture shows what may be the beginning of a historical revolution in the making. The number of actual farms was declining until 1979 when the number of farm units showed an increase in 18 states. In 1980 a total of 28 states showed increases in units or maintained the status quo from the prior year. By in large, the states showing those increases are located in the industrialized eastern states and the commercialized states of the midwest. This official documentation of the increasing number of farms appears to have a direct correlation with the population statistics discussed earlier.

Contrary to the rise in the number of farm units, the land mass in the farms continues to decline slowly with the total of 1,049 million acres in 1979 being only slightly less than the 1,052 million acres tilled in 1978. The 1980 figures relate a continuing decrease, but slowed to a rate of less than .002 percent annually. Further, small and continued annualized decreases in acreage would appear inevitable as some lands continue to be absorbed by urbanization and highway construction projects. Over the past decade the decrease has been
less than five percent.

If the change becomes a trend, as the past three years indicate may be, it will require that we re-examine our thinking and correct our projections to meet the needs of the anticipated changes.

FARM PRODUCTION

Farmers today in the United States produce three times more per work-hour than in 1960 and over twelve time as much as in 1930. Although large acreages were held out of crop production between 1960 and 1970, total U.S. farm output increased as fast as the U.S. population as shown in the graph depicting U.S Crop and Livestock Production (figure #5). During most of the 1970's acreage has been restored to production and the output continued to increase even faster than in the 1960's; however, U.S. farm output for 1980 was three percent below the 1979 level. Officials anticipate the decline to continue and recent data confirms that a similar decrease in production occurred in 1981, thereby following the patterns of the previous year. A U.S. Department of Agriculture study indicates that the production drop occurred as a result of cash crop planting being reduced by the large farm operations to permit absorption of surplus materials produced in the preceding years, in hopes of increasing prices in coming years. The crop plantings notably are not those usually associated with small farms.
Figure #5: U.S. CROP & LIVESTOCK PRODUCTION

Source: USDA Handbook of Agricultural Charts
An annual increase in farm production has come to be taken for granted, but in the early decades of this century farm production was almost on a treadmill. Agricultural production in the United States remained virtually unchanged from 1910 to 1930. It rose an average of 1.4 percent annually in the 1930's, 2.1 percent in the 1940's, 2.1 percent in the 1950's, 1.0 percent in the 1960's, and since 1970 it has an average increase of 2.8 percent.31

The chart showing U.S. Farm Productivity (figure #6) shows a decline in output in relationship to the input of labor unit. While there is a great deal of similarity of the graphs in figure #5 and figure #6, it must be noted that the reduction of production of cash crops on large corporate farms influences both the production unit and the input unit to approximately the same degree. It is also noteworthy that figure #6 shows a cyclical movement occurring each fifth year. Since 1980 represents another bottom in the five year cycle, one may project with some logic an increase in U.S. farm productivity at least through 1985.

As the farm output continues to show an increase over the unit of input, the farming business in this country should remain profitable and encourage large farm operators to accelerate large cash crop production to meet growing export needs. This will permit the newly implanted small family farms to produce the smaller consumable crops at relatively stable market prices.
Figure #6: U.S. FARM PRODUCTIVITY

Source: USDA Handbook of Agricultural Charts
Consideration has been given by the Department of Agriculture to devising a system to produce a new set of figures and graphs based upon those units producing for export and those producing for national consumption. Most likely such graphic displays would depict a continued growth of output over units in input in a more drastic increase than when using the combined U.S. production figures. This may be related to the fact that large corporate farms are mass producers of high volume export commodities.

FARM REAL ESTATE VALUES

Farm real estate prices rose about 15 percent during 1979. Through June of 1980, it appears that land values generally remained unchanged, with small increases in some regions being offset by decreases in others. For the period February 1980 to February 1981, average land value increased between 7 and 12 percent. Most of this increase occurred during the winter months when farm real estate became more active. For 1981, land value changes will be affected by prospects for net farm income which are showing a slight increase and by interest rate levels which are anticipated to remain high through 1982. These factors would tend to cause a stabilization of the land cost factors. Over the past ten years, farmland prices have increased at an average rate of 13 percent with a surge to 15 percent during the year ending in 1980. (figure #7)
Figure #7: CHANGE IN FARM REAL ESTATE VALUES

% of March 1, 1967

Source: USDA Agricultural Statistics, 1980
rate has averaged only 7.5 percent over the same period, so the constant dollar value of farmland has increased substantially.

The total value of farm real estate was $671 billion on January 1, 1980. Building values accounted for about 17 percent of this total. Over the last ten years, the total value of farm real estate has increased by 211 percent. 35 This increase reflects higher prices since the quantities of all land and buildings has not substantially changed over that period.

Net farm income is now in a declining posture. Interest rates have been high and credit often tight or not available. These factors, in addition to the adverse weather conditions, have apparently reduced activity in the farm real estate market. Federal Reserve Banks in Chicago and Kansas City reported slow-to-negative growth in farm values in their districts, while the remaining districts indicated that land values would remain stable during the coming year or two. 36

The farm lenders were surveyed in September 1980 to obtain their estimates of land price changes. In general, the lenders thought that land prices had increased an average of 5 percent since February. Land values are expected by many lenders to actually decrease if the current interest rates continue their climb or fail to decrease from their present high levels. Some lenders expressed the opinion that the country may experience a stabilization of farm ground prices that could last for
12 to 24 months, before experiencing another increase cycle.

The projected inflationary growth of land values (figure #7) will encourage future land investment programs. As the farmland value inflates, it automatically reduces the debt/asset ratio and provides opportunities for the small farmer to capitalize on additional borrowing capacities generated by the trend. This should act as an important inducement to encourage the movement to the smaller farm units, as the increased value of farm properties is substantially greater than the inflationary movement in non-productive metropolitan properties. This may give rise to speculation by small operator/investors seeking to offset payments through reductions of food costs.

FARM INCOME

The changes in the distribution of income and wealth in farming are occurring in the context of significant changes in total income. The cash income of the farming sector is comprised of cash receipts from farm marketing and any federal payment made directly to farmers for farm related activities. Farm marketings represent agricultural products sold by farmers multiplied by the prices received per unit of production in the local marketplace. Gross farm income includes cash income, value of farm products consumed in farm homes and the rental value of farm properties. It should be noted that farm income does not include: (1) farm related incomes of farmers who do not live on farms, (2) farm related incomes of nonfarm
landlords, nor (3) farm wages of hired labor.\textsuperscript{35}

Cash incomes of farmers rose steadily into the 1970's with farm earnings rising more than three times the average rate for the period of 1960 to 1962. Even with the relative adjustments for inflation (figure #8) the 1974 average was still slightly more than 50 percent above the 1965 average. This trend did, however, reverse itself in the middle of the 1970's and began a rapid decline which continued through 1977 to a low of $18 billion.

The segment from 1978 to 1981 has once again altered the previous period's declining trend. Within this period the net farm income once again began to show slight amounts of increase (figure #9) to $26 billion in 1978; $28 billion in 1979; to $30 billion in 1980.\textsuperscript{39} This period and its related increases correspond significantly with the reversal of the trend to large corporate farms which occurred in 1978. Such a numerical revision back to the smaller farming unit draws an important correlation with the net income increases appearing with that same period of time.

Projections of net income to 1985 (figure #8 and figure #9) show the expected continuation of rise in net farm income, reaching peaks unequalled in farm history.\textsuperscript{40} These increases of net farm income may provide continued incentives for the appearance and growth of the once popular small family farm unit.

Should net income continue its expected growth at a rate in excess of the inflationary cycle, it will perhaps
Figure #8: NET FARM INCOME

Source: USDA Handbook of Agricultural Charts
Figure #9: INCOME FROM FARMING

Source: 1980 Handbook of Agricultural Charts
encourage the beginning farmer to actively participate within the industry. Wages found within the general labor market normally increase only at the actual rate of inflation. This will then assure the small farmer of some degree of prosperity unattainable among the general labor force.

ENERGY COSTS

Farmers will face significant increases in the cost of energy. Decontrol of energy prices, the price of foreign imports and other factors will cause the prices paid for fuel and energy in 1982 to increase by approximately 20 percent above the 1980 costs. Such estimates allow for some price fluctuations necessary to remove current surplus fuels. This rate of increase exceeds those for most other production expenses and is a significant increase in real terms. Farmers will have to consider the types of substitutions that can be made between energy and fuel intensive crops, such as corn and cotton.

Whether or not the farmer will alter his production strategy in coming years in response to high petroleum prices will be further influenced by relative crop prices. Figure #10 reflects the increasing cost of production fuels.

While prices will be significantly higher, farmers can expect supplies of major fuels to be readily available. The national stock levels as reported by commodity reporting bureaus currently contain some excess fuels.
Figure #10: ENERGY PRICES PAID BY FARMERS

Source: USDA Handbook of Agricultural Charts
The highly seasonal needs of agriculture production and inability to recover from the lack of fuel at critical planting and harvesting periods point the need for agriculture to maintain its current priority if the need for national allocation or rationing programs should arise. The farm sector is producing at full capacity. If fuel supplies are not available, the ability to meet the growing demand for domestic consumption and foreign export will be jeopardized. Reduced output would be reflected in commodity prices and the ability to meet the objectives of maintaining stable prices at reasonable levels, maintaining export availability and international food security.

Energy consumption has continued to grow as the large farm replaces physical labor through advancement in the mechanical technologies. Since energy costs have risen at an alarming rate and will continue (figure #10 - projections) there is every reason to suspect that the labor intensive small farm will be able to produce some crops at a lower input cost than the large mechanized farm. This will encourage the re-establishment of the smaller and more highly specialized farm units.

A secondary result of the rise in energy prices has a direct bearing on the transportation/final market price. It is generally an accepted fact that major corporate farms are situated at greater distances from the market place than small farms. This is true because part of the efficiency of the large farm is its ability
to cultivate large contiguous land holdings. As small farms are established closer to the markets of large metropolitan areas, they will automatically enjoy the advantages of reduced energy costs for transportation.
SECOND CONCLUSION

Analysis of the historical trends and the review of projections in U.S. farming trends allude to another revolution in the business of agriculture. It becomes increasingly evident that the structure of farming in this country is about to experience a new series of profound changes. The beginning of the transformation is seen in the social and economic conditions providing fertile ground which is encouraging the rebirth of the small family farm.

As noted, the slight rise in the total farm population which began in the years 1978 and 1979 represents the first real change since 1935. The increases which are expected in income levels and property values are the inducements that enterprising young people are seeking, and the ability to produce food and fiber for one's own consumption and surpluses to provide for others becomes a matter of self fulfillment. The outlook for the future is indeed bright, and it does provide the incentives and motives for establishment of small family farms in this country. The projections suggest that the movement may be sustained for many years.
CHAPTER III

PROPOSED REVISIONS TO THE FARMERS HOME ADMINISTRATION
INTRODUCTION

Over the past 40 years, our agriculture policies have been directed primarily toward maintaining reasonable incomes for the nation's farmers and supplying the American consumer with an abundant supply of high quality food and fiber at fair prices.

While some persons have criticized our farm programs for various reasons, we can be proud of the achievements of American agriculture. For example, net farm incomes reached a record high in 1979 of over $30 billion: at the same time, consumers spent less than 17 percent of their disposable income for food.\textsuperscript{43}

It is my view that the family farm is the heart and soul of American agriculture and the primary reason why each of our farmers is able to feed and clothe about 75 individuals and together export over $20 billion in farm product each year.\textsuperscript{44} The number of farms in the U.S. has declined markedly since 1940. As they declined in number they increased in size and efficiency. There was a rising fear that the traditional family farm was marked for extinction, and the structure of the farm and agriculture became a matter of growing concern.

Congress recognized these concerns in the Food and Agriculture Act of 1977. As stated in section 102(a) of
the 1977 Act, "...the maintenance of the family farm
system of agriculture is essential to the social well-being
of the nation and the competitive production of adequate
supplies of food and fiber."\textsuperscript{45}

Coincidental with the passage of the 1977 Act, the
first signs of change were noted in the structure of the
American farming unit and the migration to the city began
to reverse. It is this new change in our agricultural
society that must be nurtured and assisted to guarantee
its continued expansion.

The single most important ingredient to the survival
of the new trend to return to the family farm unit is the
ability to obtain financing in sufficient amounts over
a period of time adequate to provide a liveable return of
the investment and support the repayment thereof. The
examination of the lending institutions will show that
risk or venture capital is still committed largely to the
corporate farm entity. This is particularly true in the
private segment of the banking industry. While government
programs of finance have been designed to assure the farmer
a reasonable income and the consumer a reasonably abundant
supply of food and fiber, there are serious shortcomings
and imperfections which have curtailed the effectiveness
of those programs.

I believe that improvements can and must be made
without abandoning the program approaches that have
proven themselves in the past. Attention must be given to
new issues of the time while formulating adjustments to current lending practices. These issues include the impact of inflation on farm incomes, land values, availability of credit, cost of production and the adequacy of our rural development programs.

As will be shown, the institutions created to assist agricultural development in this country continue to perform that function once the farm unit has been established and operating successfully. Only the Farmers Home Administration retains the commitment to the beginning farmer, and even that trust is being seriously eroded. With high initial investment costs, only by accident of birth or death is an individual in a position of becoming a new member of the rural community. This section will suggest how revisions to the Farmers Home Administration would restore its original purpose by changing the functions and the criteria which guide the department in its task.
DEBT FINANCING SOURCES

By 1940, the basic organization, structure and operating characteristics of the financial markets and institutions serving the farm sector were all well established. Changes occurring since 1940 were designed to further refine the structure, enhance its efficiency and adapt its lending practices and policies to the changing characteristics of the farming industry.

Major sources of debt capital for farmers have included (1) commercial banks, (2) the Farm Credit System, (3) life insurance companies, (4) U.S. Government lending services, (5) trade firms, (6) individuals, especially for sellers of farm real estate, and (7) other lenders. The first four categories are considered "financial institutions" because they either specialize in lending or have specialized loan programs for farmers. The remaining three sources are considered as non-institutional. "Other lenders" may include savings and loan associations, credit unions and other such organizations although their volume of lending has played a very minor role. Although these sources of debt capital have been available since 1940, their roles, rates of growth and market shares in farm lending have changed considerably since then.46

The proportion of farm debt held by the commercial banking system rose from 15 percent in the 1940's to peak at 29 percent in 1952 only to level off and retain that
same percentage through the next decade. A rise was experienced which peaked in 1974 when it reached 31 percent of the market share available. Commercial banks then began to experience liquidity problems as evidenced by high loan-to-deposit ratios and began to reduce their farm loan activity. The commercial banks currently enjoy about 11 percent of the market.

The Farm Credit System by 1940, had developed into an organization of seven district Federal Land Banks, Banks for Cooperatives and Production Credit Associations incorporating the lines of supervision and controls we see in existence today. Periodic revisions in the system, especially in the Farm Credit Act of 1971, have substantially altered the lending policies and programs. These changes permitted the form of intra-system coordination needed for the institution to maintain its credit worthiness in the financial markets while allowing it to make lending adjustments corresponding to new farm needs. Accordingly, the changes within the farming sector dictated growth of corporate farms, and the new credit act permitted the Farm Credit System to devote a greater share of its funding to satisfy the debt requirements of the corporate entities. As the demand for new capital grew, the market share retained by the Farm Credit System also grew to now exceed 36 percent, and is to a large degree confined to large loans to large corporate farms.

The Federal Land Bank, a division of the Farm Credit
System, served the function of being the refinance market in the 1940's for the debt stricken farmers emerging from the depression years. The high income level of farms following World War II allowed substantial debt reduction. All during this time the Federal Land Banks retained their relatively conservative posture of lending. As the farm lending needs increased to meet the needs of financing for acquiring additional lands as farms increased in size, less monies were devoted to the smaller farm operations. With current trends indicating a return or a re-entry of small farm units, the Farm Land Banks may readjust their lending practices to include consideration for farmers entering the agricultural scene.

The Production Credit Associations (PCA's), also a division of the Federal Credit System, exhibited steady growth in their market share of non-real estate farm debt. In 1940 the PCA's contributed only 2 percent of the capital debt financing, and have increased their market share to approximately 30 percent today.\(^5\)

Life insurance companies have a long history of supplying large amount of long term debt capital to farmers. Their market share climbed during the 1940's and early 1950's while the Credit Banks were experiencing a reduction. A decline evidenced itself in the late 1960's as the insurance market began to feel the effect of changes within its own product sales from whole life products to term life insurance. This decline continues to this day and
is expected to continue. Within the past five years insurance company policyholders have made strong demands upon the loan equity in their policies. This may be explained as the interest rates for policy loans are now well below those rates currently being charged by the commercial and private lenders. Life insurance companies in general now contribute less than 15 percent of the capital available to farm units.

Data on trade financing is much less precise than the data available for institutional lenders, however, the role of trade financing appears to have greatly declined since the late 1960's. In contrast, financing supplied by individuals, especially sellers of farm property, has appeared to maintain a relatively stable share of the market.

Farm lending by the U.S. government takes several forms. One consists of nonrecourse price support loans and crop storage loans, as made by the Commodity Credit Corporation as part of the government's price and income policies for farmers. These loans were relatively high during the 1940's and the early 1950's. They then began to decline as government programs were modified to allow greater movement of commodity prices, and to reflect increasing reliance on direct payments as a means of income transfers for farmers. Loans by the Commodity Credit Corporation began to increase during periods of low farm income.
The Farmers Home Administration (FmHA) is a governmental lending agency operating in the U.S. Department of Agriculture. FmHA was formally established in 1946 to replace earlier government lending programs, with the purpose of continuing to provide supervised credit to farmers who are unable to obtain credit from any of the commercial lending institutions at reasonable rates or terms. In this sense the FmHA is obligated to maintain the strengths of the family farm structure by providing loans for those farmers in desperate need and for young beginning farmers. Despite these commitments, the FmHA appears to have strayed from its original purpose. Recently the FmHA has been sharply criticized for not following the reductions in prime interest rates, while other institutions have lowered rates of interest to reflect the prime rate reductions. Senate hearings are now being scheduled to review this situation and it has been suggested by some that the agency be disbanded entirely. The FmHA now has less than 8 percent of the farm lending market.

It cannot be argued that the lending facilities of the private and governmental sections have failed to respond to the debt requirements of the farming industry. As the forces of production and technological advancement gave the opportunity to increase the relative size of farms, it also related increased capital requirements which these institutions responded to by directing more and more capital to the large farm operation. This allowed
the farmer to maximize his ability to produce surplus commodities for consumption in this country and abroad. It can be debated with success that these actions led to a decline in capital availability to the small farm unit, thereby curtailing the growth of small farms. With trends of increased small farm activity, a revision of the FmHA commitment may well be the initial step to encourage this movement. If the FmHA could be redirected to supply needed capital to the upcoming small family farmer at a competitive rate, it could also provide encouragement for commercial markets to become competitive.

Figure #11 and figure #12 are provided to graphically illustrate the percentage of participation by the various lending agencies in both the field of real estate and non-real estate lending.
Figure #11: WHO HOLDS FARM DEBT (REAL ESTATE)

Source: USDA Handbook of Agricultural Charts
Figure #12: WHO HOLDS FARM DEBT (NON REAL ESTATE)

Source: USDA Handbook of Agricultural Charts
RECOMMENDED CHANGES TO FmHA

The FmHA, as a governmental agency, functions with tax dollars to promote agriculture in the United States. Its staff is farm oriented and the distribution of its services encompass the entire nation.

Over the past years this organization has performed a useful and a needed function. As with all organizations, there comes a time when changes are needed to meet the requirements of the society which they serve. The FmHA is currently the subject of criticism and perhaps now is the proper time to investigate a series of changes and recommendations which would revitalize it purpose.

PURPOSE AND LENDING CRITERIA

The formation of the Farmers Home Administration as indicated previously was expressly to provide the necessary credit need of the farmers not being met by other lenders at reasonable rates and terms. Since its formation in 1946 nearly every element of the economy has changed significantly or disappeared in total.54

The purpose or the mission of the FmHA must be restructured to a program that is more definitive in description. We all tend to question the reasonability
of interest levels of 20 percent or short term repayment schedules with large balloon final payments.55

In view of the continuing criticism of the FmHA, a change in objectives could preserve this organization of specialists and redirect their energies to the benefit of the agricultural community.56

I recommend that the purpose be redesigned in the following manner: The mission and the objective of the Farmers Home Administration shall be to encourage the growth and development of the small family farm through providing investment funding at rates and terms which encourage entry into the business of agriculture.

This purpose shall be further defined as lending assistance in obtaining funding from the private sector in conjunction with funding obtained through this agency.

The criteria for lending shall be restricted to the creation, and not the continued maintenance, of new small family farms. Individuals currently engaged in the field of agriculture as it relates to the production of crops or livestock human consumption shall not be eligible for assistance. Existing farms should seek operational funds in the private sector. Applicants for loans will be required to present a formula by which they can show sufficient income generation to provide income to support themselves and family derived entirely from the output of the farm property intended to purchase.

This type of purpose outline will insure that the
agency will not stray from its intended design. The purpose will restrict the agency and make it more efficient in its operation.

ORGANIZATION

The Farmers Home Administration in its present form is massively overburdened with inefficient management systems. At present it maintains a series of 1500 individual offices to serve the agricultural counties throughout the country. Each office is staffed by a minimum of an administrator and a secretarial staff. The system requires further that each office will maintain a loan approval committee consisting of three persons.

At a minimum this develops into a system employing over 7500 individuals as a field force for servicing of $6.6 billion in farm real estate loans. Statistically this make the FmHA the most labor intensive banking system in the country if the ratio of staff personnel to loan amount is examined. This is not taking into consideration the Washington based staff and officials.

The staffing system was established at the time the Farm Act in 1946 was implemented, and no substantial revisions have been made since that time. Since the staffing requirements were set by law and regulation, it is time to re-examine those requirements. Private enterprise has utilized modern technology to increase its
operating efficiencies and promote better utilization of its personnel. The FmHA has been burdened and encumbered by the regulations of staffing.

I recommend that consideration be given to the reduction of servicing offices. In 1940 perhaps this requirement of local offices was needed to assist the farmers. Telecommunication and computer technology must be utilized in the consolidation maneuver to promote maximum efficiencies. With the new modes of transport and communications the consolidation of the present 1500 county offices could be reduce to as few as two regional offices per state, providing those offices are separated by more than 150 miles.

The consolidation of offices from local to a regional basis would permit some reduction of personnel. The present staffing of over 7500 people gives rise to the comparison of the number of loans made to farmers. In 1979 a total of 56,383 loans were made to individuals including some 24,568 emergency loans. This translates into only 7.5 loans approved per staff person in the system per year. If the present system is reviewed including all loans of every nature made by the FmHA during 1979, the ratio does not exceed one loan approval per month per staff person. Even if consideration is given to the servicing of outstanding loans, the private sector of the banking industry could not survive with this loan to staff person ratio.
The proposal in total will also effectively reduce the responsibility of the FmHA as its purpose will be re-defined. Action should be initiated to streamline the agency into a more viable tool to promote the expansion of the family farm unit through availability of immediate capital for purchase and operations.

REVISED DEFINITION OF SMALL FARM

The family farm, as a definition, was constructed by the U.S. Department of Agriculture (USDA) as early as 1935. This definition reflected the consensus of the times when the USDA described the family farm as "a farm on which the operator, devoting substantially full time to operations, with the help of other members of his family and without employing more than a moderate amount of outside labor, can make a satisfactory living and maintain the farm plant". It is obvious that as the system developed technically and became mechanically efficient that the majority of farms in the country would qualify for services of the agency by definition. The definition would include large operations in terms of capital and land, but would exclude the bottom side of the spectrum such as part time units, residential farms and farms that could not provide reasonable incomes for their residents. This definition became a liability to the bureau and was revised in the 1950's.
In its place appeared a family farm definition that continues to be used today. A version of the new definition presented in the early 1970's read:

The essential characteristics of a family farm are not be found in the kind of tenure or in the size of sales, acreage or capital investment, but in the degree to which the productive effort and its reward are vested in the family.

The family farm is a primary agricultural business in which the operator is a risk-taking manager, who with his family does most of the farmwork and performs most of the managerial work.62

This definition then included the bottom of the spectrum by recognition of marginal farms, part-time farms and residential farms and totally eliminated the idea that the family farms had to be an economically viable entity.

In order to fulfill its objective of assisting the beginning farms, the definition must be changed to reflect and limit that charge. I suggest that the following definition more appropriately defines the system which the FmHA was orginally formed to assist.

The essential characteristics of a family farm shall not be related to tenure, size of sales nor acreage or capital investment.
The family farm is an agricultural business from which the operator and his immediate family shall maintain a satisfactory living (income) through full time operation of the farm unit, exclusive of all other sources of income.

For the purpose of obtaining funds from this agency, such family farms shall not have been operated by the applicant or any other member of his immediate family for a period of more than two years.

Such a definition by its very nature would exclude the established farm units and again eliminate the marginal and purely residential farmers from obtaining funds for the purpose of establishing a new family farm unit. As one may observe, this proposed definition is limiting in nature whereas prior definitions were an obvious attempt to encompass all farming activity in the United States. Prior definitions defeated the initial purpose of the department.

The change in definition of the small family farm for purposes of lending by the FmHA purposely excludes existing farms. There are sufficient private lending institutions and sources to provide capital once the farm unit is established.

INTEREST

One of the major complaints lodged against the
FmHA has been its inability or its wanton refusal to maintain the interest rates charged to its customers at levels equal to or below the prime lending rate. In recent meetings of the U.S. Senate Subcommittee on Agriculture Credit the presiding officer, Senator Patrick Leahy, threatened that the agency should be disbanded if it is not able to maintain the cost of borrowing at levels of prime interest or below. He pointed to the ridiculous situation when the rates imposed by the FmHA exceeded the prime lending rates by as much as 4 percent.63

Senator Melcher of Montana expressed amazement at the FmHA clinging to high interest rates when agriculture is in trouble and detailed several instances when rates charged by the agency exceeded the rates on commercial paper by as much as 6 percent.64

It must be recognized that the rate of interest charged by this agency is set by law, and is therefore slow to reflect or respond to changes in the financial market. Loan limit maximums are also established by law, and these limits help assure that funds are available for a relatively large number of borrowers.65

Regulations and changes in the laws are required if the agency is to meet the need for loan capital as detailed by the new definitive purpose of the agency.

The ability to fluctuate the rate of interest must be revised to reflect more closely the interest rate being charged in the private sector of the economy. This
is not to imply that those rates should be identical. When reminded of the purpose of the agency it becomes apparent that the rate of interest should be established slightly below the prime rates. This will encourage the borrower to become engaged in the farming occupations. Proposed legislation must remove the option to raise or lower a rate of interest once established, as reflected in the current law. The purpose of the FmHA is not to produce a profit from its operations.

The interest rate level should be set as a specific percentage below either the prime commercial lending rate or the rate of interest charged by the Federal Land Banks for the purposes intended. While this level would not create a competitive situation with the private sector, it would not create a hardship when the new farmer is required to approach that private sector to obtain additional financing or capital.

There will be concerns of equity which will outweigh the concerns for economic efficiency, however, it must be remembered that the FmHA programs are to be designed to help the individual become established in the business of farming.

LAND USE POLICIES

The nation's land resources are important and irreplaceable assets. Land and water are central
ingredients in the processes involved in producing food and fiber commodities. Patterns of land and water use are consequently at the core of continuing policy deliberations over the structure of the American agricultural system. Their wise management is among the more pressing matters on the public agenda.

Conversions of farmland to essentially irreversible use are occurring through the development of suburban areas and the expansion of highway and arterial systems. They often involve resources that are uniquely well suited to the production of the food and fiber commodities essential to this country's social and economic well-being. Farmland additions also occur, but they often entail major investment in land improvements and can generate environmental side effects.

I would suggest that a system of land classification of agricultural grounds be initiated. I acknowledge that land classification is a primary responsibility of the United States Department of Interior. Without infringing upon that authority, the Farmers Home Administration should encourage the promotion of land use classification and zoning.

The recent attempts by the government to classify and dictate land use principles of government held property caused an uproar by conservationists and industrialists. A system to reclassify or simply designate certain properties is essential to the perpetuation of agriculture in this
country. Although the ownership of property is cradled in the right of eminent domain, we find that zoning in metropolitan areas is deemed to be beneficial to the lifestyle. If this same logic can be applied to the rural segment of the country, I would envision that a system of zoning or of classification would be possible.

Providing agricultural lands could be so classified, a means of disincentives could be established to prevent or at least reduce the rate of loss of productive grounds. A system so simple as to disallow the capital gains tax application from sales of farm ground if such sale did result in a change of land use to a purpose other than crop or livestock production would be effective. This in effect would not prohibit the right of property owners to dispose of property, but would reduce profits from sales and add costs for those who elected to change the land use. I would not foresee the necessity to require formal hearings to change that usage.

Such a practice would also have a tendency to stabilize the inflationary rate we acknowledge in the price of farm and productive land. The secondary effect would be that non-productive lands would then be utilized for the expansion of suburban development. It would also force all governmental and municipal entities to explore the greater use of nonproductive lands for use in the development of highways and recreational facilities.
THIRD CONCLUSION

As the restructuring and redesign of purpose is further refined and expanded through the legislative body of the Congress of the United States and the U.S. Department of Agriculture, the Farmers Home Administration will become a functioning agency of this government.

No single revision proposed will or can unto itself accomplish the revitalization of the agency. Although the FmHA has served a useful objective, it was allowed to become a cumbersome and ineffective organization. This is not to detract from the many favorable accomplishments over the past 25 years. Other agencies such as the Federal Land Bank system which have had their origin within the government are now capable of sustaining the credit needs of the established agricultural community. Private lending institutions and individual lenders should not have to compete with government agencies dealing with funds which are generated by taxation of the American public.

The change in position of the FmHA will not act to compete, but rather will provide a source of risk capital or venture capital not generally solicited by the private sector. The program as I propose it would assist only in creating new clients for private lenders in the future.
FINAL CONCLUSION

Statistical measures of income and standard of living show rural people at a disadvantage, but on the basis of less tangible standards and values, many rural people prefer to remain in nonurban areas. Since the late 1970's, they are being joined by people from urban areas who want to escape the crowding, noise, pollution and crime in the city environment. Many rural people believe that the uncrowded environment is beneficial for family life and the rearing of children. Many farmers cherish traditional rural values such as the opportunity for independence. Some farm people believe that the art of agriculture is man's fundamental employment upon which other economic activities depend and are convinced that farming is a natural life style and therefore is a good life.

Perhaps the admonitions of Goldsmith and Mrak have been unconsciously heeded by the American community, and the disasters which haunted the societies of the world in the past will be avoided. For the first time, a trend has turned before the catastrophe forecast affects each of us. We have recognized the need of agriculture. The city dweller has found need to return to the land and we have rediscovered the strength and the pride that the
stewardship of the land affords us.

With the proven and projected return to the family farm unit, we are faced with the challenge to sustain and nurture the movement by the creation and revision of influencing forces, the most important of which is the ability to create a favorable economic climate to foster the growth of agriculture.

The Farmers Home Administration is the established and natural vehicle to use in the promotion of small farm development in this country. The recommended changes of purpose, mission and function should be implemented to provide the tools to effectively cultivate the growth of the small family farm. This country would then reap the harvest of those efforts.
NOTES


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6. Ibid., p.114.

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