American Farm Credit System (FCS) and Its Enlightenment

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Abstract. Credit is an important factor affecting agricultural output, but the problem of financial constraints in rural and agricultural development in China is highlighted. How to develop and improve the agricultural credit system is of great significance to the healthy development of China's agriculture and the integrated development of urban and rural areas. This paper reviews the development history and organizational structure of the American Farm Credit System (FCS), analyses the differences between it and China's agricultural credit system, and puts forward some suggestions on how to build and improve China's agricultural credit system from enlightenment.

1. Introduction

Since the Reform and Opening, China has entered a period of rapid economic development and has achieved remarkable achievements. However, the development of China's agricultural finance has lagged behind the overall economic development. With the development of industrialization and urbanization, the difference in urban and rural economic development has gradually widened. In addition, the profitability of credit funds has made the funds tilt to other industries, and the problem of financial constraints in rural and agricultural development has become more prominent. In recent years, the total value of credit to agriculture has increased year by year, but since the year of 2008, their share of total credit has been decreasing (Figure 1). In 2016, the added value of China's primary industry accounted for 8.56% of GDP, while the balance of agriculture, forestry, animal husbandry and fishery loans accounted for only 3.37% of the total balance of various loans, the balance of the farmer's loan accounted for 6.51%, and the availability of formal credit for rural households is less than 30%, which indicates that China's current credit support for agriculture is insufficient and has not fully played its due role. However, credit has long been an important factor affecting agricultural output and an indispensable factor in measuring the urban-rural gap. Therefore, the development and improvement of the agricultural credit system is of great significance to the healthy development of China's agriculture and the integrated development of urban and rural areas.

At the beginning of the 21st century, American agricultural credit also experienced similarities with Chinese agricultural credit. The proportion of credit to agriculture plummeted between 2001 and 2004. However, what is different is that the number has stabilized in the following years (Figure 2), and agricultural added value accounts for a much lower proportion of GDP than this. In 2016, the added value of American primary industry accounted for 0.95% of GDP, but the balance of agriculture, forestry and fishing loans accounted for 6.67% of the total balance of various loans, showing that American credit has strong support for its agriculture, which largely comes from the Farm Credit System.

2. American Farm Credit System and Its Development

American Farm Credit System (FCS) is a national network of borrower-owned lending institutions that provides credit to American agriculture established by the US Congress. It provides short-term, medium-term and long-term loans, machinery leasing and related services for farmers, pastoralists, aquaculture farmers, forest harvesters, other agricultural-related practitioners and rural landlords[1-3]. In 2016, FCS provided approximately 41% of the loans to American agriculture, second only to major commercial banks (42.2%), being an important source of credit for American agriculture (Figure 3).
FCS has gone through a long period of development and improvement to become a farm financial professional service network of mutual assistance and cooperation integrating banking system, credit association and fund company now (Figure 4)
2.1 Initial Formation Stage of FCS (Early 20th Century-1916)

At the beginning of the 20th century, with the end of the Western Development, the land was exhausted, and the increasing population made the demand for agriculture rising. In 1910, the total population of the United States reached about 91 million, more than half of which was rural, resulting in huge credit demand. However, at that time, the amount of agricultural credit supply in the United States was small, the loan period was short, and the interest rate was relatively high. The limited credit supply could not meet the demand for agricultural development, and finally prompted the United States to establish its unique agricultural credit system.

The low return on investment and the high risk of agriculture are destined for the need for government involvement. In 1908, the Rural Credit Commission proposed the establishment of a cooperative credit system to provide credit funds to farmers and pastoralists. Subsequently, the United States set up a special committee to conduct research on the development of agricultural credit in European countries, and submitted the *Preliminary Report on Land and Agricultural Credit in Europe* in 1912. In 1913, President Wilson formally proposed a plan to establish a rural credit system. In 1916, the US Congress passed the *Federal Farm Loan Act*, which marked the formal establishment of American farm credit system. It not only built the framework of FCS, but also established a top-down three-tiered organizational structure: the Federal Farm Loan Board, the Federal Land Banks, and the National Agricultural Loan Association. The act divided the country into 12 farm credit districts. The federal government funded one Federal Land Bank in each district and promoted farmers to establish grassroots agricultural loan cooperatives. The Federal Land Bank first decentralized funds to agricultural loan cooperatives, and farmers got loans from the cooperatives in which they participated. At the same time, the act also clearly stipulated the functional scope and election rules of each organization, the details of equity subscription, loan interest rate, lending process, repayment responsibility, repayment method, etc. [4].

2.2 The First Boom Stage of FCS (1917-1922)

The establishment of the Federal Farm Loan Board marks the beginning of the first boom in FCS. At the end of 1917, there were 1,839 national agricultural loan cooperatives established and 1,985 under construction, and the total credit demand has reached 2 billion dollars. Another data showed
that there were 4,018 national agricultural loan cooperatives established in 1919, and by 1922, about 74,000 farmers had borrowed 234 million dollars from the Federal Land Bank.

2.3 Developing Stage in Difficult Situations (1923-1933)

Although the adoption of the Federal Farm Loan Act allows farmers to obtain their production funds through land mortgages, the repayment of borrowing needs to be based on the profit of selling after harvest. With the end of the First World War, the demand for food products was drastically reduced, and the price of agricultural products fell sharply, affecting the profitability of farmers' sales. At the same time, banks and suppliers of production materials and services urged farmers to repay when crops were just ripe. Coupled with the competition of similar agricultural products, farmers were always forced to repay their products at a lower price. It also affected the realization of the real market value of agricultural products. In order to change this situation, the US Congress passed the Agricultural Credits Act (1923) to provide financial support to farmers in the selling period. According to the act, the US Federal Ministry of Finance established the Federal Intermediate Credit Bank under the Federal Land Bank to provide preferential credit services to commercial banks and agricultural companies. The act also allowed private establishment of the agricultural credit corporations, which provided medium-term loans to cooperatives engaged in the selling of agricultural products, and provided discounting and rediscounting services to other financial institutions. Together with the Federal Reserve Bank and commercial banks providing short-term loans, and the Federal Land Bank and Joint-stock Land Bank providing long-term loans, FCS had basically developed into an agricultural credit system with short, medium and long-term loans.

The above measures injected a booster into the development of American agriculture at the time. In 1929, the Federal Land Bank provided $1,198 million in loans to agricultural production. Subsequently, the United States suffered the Great Depression. The Congress immediately passed the Agricultural Market Act to stabilize agricultural land prices and support the development of agricultural organizations. However, affected by the economic crisis, American farm credit system has still been hit hard. At the end of 1932, the amount of loans from the Federal Land Bank fell to $117 million. In 1933, nearly half of the country's agricultural loan cooperatives ceased operations, and FCS could not provide substantial support. At that time, the bonds of the Federal Land Bank and other agricultural financial institutions were largely unsalable, and it was difficult to raise sufficient funds, which made the farmers difficult to borrow money, then the production capacity and profitability decreased, and it was difficult to repay the loans. A large amount of collateral was confiscated, and banks could not quickly sell collateral, resulting in a large backlog of useless collateral.

In order to save the agricultural finance and agricultural production in trouble, the Roosevelt New Deal introduced a series of bills and measures. In 1933, President Roosevelt signed a decree to establish the Farm Credit Administration to govern the nation's agricultural credit affairs. In the same year, the US Congress passed the Emergency Farm Mortgage Act, injecting large amounts of funds into the Federal Land Bank and lowering interest rates to refinance agricultural production. In addition, the Congress passed the Farm Credits Act (1933) and established two new types of financial institutions that provide short-term loans for agricultural production and sales. One type concludes the Production Credit Corporation and the Production Credit Association, and another type is the Bank for Cooperatives. This series of acts and measures marks the maturity of the American Farm Credit System.

2.4 The Second Boom Stage of FCS (1934-1987)

The above-mentioned series of acts and measures have saved the troubled American agricultural finance and production. After the test of the economic crisis, the American farm credit system achieved prosperity again for a long period of time. In the 1950s and 1960s, the United States gradually adjusted the FCS to better adapt to the development of agriculture. For example, in 1953 the Congress passed the Farm Credits Act (1953) to separate the Agricultural Credit Administration from the Ministry of Agriculture. Later, the FCS's leaping development was related to two major changes in the late 1960s and mid 1980s.
The first major change occurred between 1968 and 1969. In 1968, FCS redeemed all the shares held by the government, which truly became the institution owned by the borrower and operated independently. In 1969, the National Services Commission on Agricultural Credit was established. Its main task was to examine and evaluate the development status of the FCS and propose reforms. This change is the biggest change to the FCS since 1933.

The second major change occurred between 1985 and 1987. In 1985, the US Congress passed the *Farm Credits Act (1985)*, separating the Agricultural Credit Administration from the FCS, making it an independent regulator. In 1987, the Congress passed another *Agricultural Credits Act (1987)* to provide loans to troubled agricultural financial organizations, established Farm Credit System Insurance Funding and Federal Farm Credit Bank Funding Corporation, and merged the Federal Land Bank and its federal mid-term credit bank, greatly improving FCS’s structure.

After two major changes, the profitability of FCS has improved significantly since the 1990s. Then FCS internally carried out some institutional streamlining and mergers, which further improved the efficiency of FCS and promoted the development of American agriculture. Even after the economic crisis broke out in 2008, the efficiency of FCS is still steadily increasing. At the end of 2008, the FCS accounting net income for the year was $29.2 billion.

3. Comparisons and Differences Between American Farm Credit System and China's Agricultural Credit System

3.1 Differences in Policies and Institutions

3.1.1 Differences in Degree of Legalization

Since the establishment of American Farm Credit System, every change in it has been supported by legislative documents passed by the Congress or decrees signed by the President, including *Agricultural Market Act* in 1929, *Emergency Farm Mortgage Act* and *Farm Credits Act* in 1933, *Farm Credits Act* in 1953, 1971 and 1985, *Agricultural Credits Act* in 1923 and 1987, and so on. Every institutional adjustment, functional changes, administrative measures, and policy implementation have detailed and systematic legal documents. Under such a legal level, FCS's hierarchical structure is clear. Different departments have clear authorities with high efficiency.

Compared with the US, China's financial system legislation is relatively backward, lacking relatively complete and systematic laws and regulations, and has been in the process of "promoting ideas—experimenting with implementation—reforming design—issuing documents", resulting in lack of high legality in China's agricultural credit system. Moreover, the existing legal basis of China's agricultural credit system is mostly departmental rules and regulations, local management measures, etc., and there are few laws and regulations specifically targeting agricultural credit. Like in 1977, the "Regulations on the Rectification and Strengthening of Banking Work" incorporated agricultural credit cooperatives into a unified management system; in 1998, the "Illegal Financial Institutions and Illegal Financial Business Activities Banning Measures" proposed to supervise various types of agricultural credit; in 2008, the "Guidelines for the Approval of Village Bank Establishment" guided the establishment and approval of village banks. The conflicting conditions of different support clauses and the overlapping of powers and responsibilities of various departments have also occurred from time to time, making the efficiency of China's credit support for agriculture not high.

3.1.2 Differences in Government Intervention

From the establishment of FCS, to the drafting and revision of various laws, to the adjustment of the powers and responsibilities of various departments, and to the intervention of special situations, the US government has actively but appropriately participated in it. For example, the US government organized an expert delegation to visit Europe and did a lot of research work before the establishment of the FCS, set National Agricultural Credit Service Committee to examine and evaluate the development status of the FCS and propose reforms, etc., always leading FCS to the right developing direction according to actual situations. Again, in the event of an economic crisis and special circumstances, the government can provide financial support for the FCS to ensure its
normal operation; in the event of poor economic situation, the government can provide low-interest loan concessions to allow agricultural financial institutions to tide over the difficulties. And the US government will never set foot in specific business areas that do not require government involvement.

The Chinese government’s intervention in agricultural credit is also very strong. Even in the case of the global economic crisis, it can promptly introduce corresponding policies and provide strong financial support, so that various agricultural enterprises and financial institutions can overcome difficulties. However, compared with the intervention of the US government, Chinese government’s intervention is broader and stronger, and it has already involved specific operational operations, which is not conducive to the long-term development of China’s agricultural credit system.

3.2 Differences in Organizational Structure

3.2.1 Differences in Independence and Status of the Regulatory Body

American Farm Credit System has a completely independent regulatory body: the Farm Credit Administration (FCA), which was established in 1933. It was independent from its affiliated Ministry of Agriculture in 1953 and was completely independent from the FCS in 1985. Its status is equivalent to other administrative agencies under the federal government.

In contrast, the regulatory body in the Chinese agricultural credit system is a division of China Banking Regulatory Commission, and its supervision of agricultural financial institutions is no different from that of other commercial banks.

3.2.2 Differences in Diversity and Cooperation of Operating Agencies

American Farm Credit System consists of three major systems: the banking system, the credit association, and the fund company. It consists of a number of operating agencies including Agricultural Credit Bank, Cooperative Bank, Federal Land Credit Association, Agricultural Credit Association, Bank Finance Corporation, Agricultural Mortgage Corporation, and so on. And FCS is a system with strong cooperative autonomy. The Farm Credits Act (1971) clarifies that FCS is a cooperative agricultural credit system of farmers.

China's Agricultural Credit System only has banking systems—policy banks, commercial banks, and cooperative banks. However, only policy banks and commercial banks have developed relatively better. The total cooperative autonomy is weaker.

4. Enlightenment and Suggestions on Improving China's Agricultural Credit System

First of all, accelerating the reform of the land property rights system is a prerequisite. Only by ensuring the mortgage rights of the land can the land's capital attributes be released and agricultural and rural financial markets activated. In America, Farm Credit System is based on the privatization of agricultural land, and its land circulation market is complete. Land ownership and management rights are the main collateral for agricultural credit. However, in China, agricultural land has long been regarded as non-collateral. Even after the Third Plenary Session of the 18th CPC Central Committee proposed that land contractual management rights should be regarded as property rights, it is still very difficult for farmers to obtain loans from formal channels. The availability of formal credit for rural households is only 29.4%, and 65.8% of households prefer private lending (Data source: China Rural Family Development Report 2017). China's agricultural credit system still has a long way to go.

Secondly, a sound legal and regulatory system is the fundamental guarantee for the long-term development of the agricultural credit system. At the beginning of the birth of the American Farm Credit System, it focused on the top-level design and established it under the highest level of national legal norms, providing a systematic legal basis for agricultural credit. In contrast, China lacks the top-level laws and regulations specifically for agricultural credit, and needs to develop and improve the legal and regulatory system to provide legal support for the development of agricultural credit.

Thirdly, the role of the market mechanism is an inevitable requirement for the sustainable
development of the agricultural credit system. Nowadays, the key to the construction of the farmland mortgage loan system in China is undoubtedly to give full play to the government's support role. However, with the deepening of relevant construction, the government should gradually withdraw from the specific construction and business fields and give full play to the basic role of the market in resource allocation.

Last but not the least, further improving the organizational structure of the agricultural credit system and achieving diversification and diversity is a developing direction. The government should support the development of rural credit cooperatives, rural banks and other cooperative banks, and help to establish intermediaries engaged in agricultural insurance, credit guarantees, and farmland transfer services.

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Reference


