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Business

The latest blow to struggling family farms: Rising interest rates

by Heather Long June 1 Email the author

Shane Merrill lives in a small town in South Dakota that's 1,400 miles from Wall Street, but he watches the numbers as avidly as the traders.

Merrill isn't an investment manager. He's a family farmer. Right now, as he drives a tractor and planter to get soybeans in the ground, he's also checking financial news on his smartphone. He's worried, he says, about interest rates shooting up.

To keep his farm going, he has to borrow about $1 million a year from the bank, a common scenario for family farmers. Merrill takes out a loan in the early spring to buy seeds, fertilizer and fuel and aims to pay it back, with interest, after the fall harvest.

His local bank currently charges him 5.75 percent interest on the loan, a bit higher than the national average on a home mortgage. But his rate is almost certainly going to rise, an extra expense as farmers are getting the lowest prices in years for their crops.

The Federal Reserve has signaled that it will probably raise its benchmark interest rate at least five more times by the end of 2019. As the Fed boosts rates, banks charge more for credit card debt, car loans and home mortgages. Farmers like Merrill could soon face rates of more than 7 percent.

The prospect of higher rates has locals on edge in Merrill's hometown of Parker, S.D. As they gather for coffee at Jim's Farm and Sporting Supply on Main Avenue, they talk of a "lost generation" of farmers who will go bankrupt if crop prices stay down and interest rates keep ticking up.

"It's one more burden for us at a time when our prices are half of what they were five years ago," Merrill said.

A 25-year-old with a quick wit, Merrill is the sixth generation of his family to farm the vast prairies of the Great Plains. He works alongside his dad, Allen, and his grandfather, Bob, on a large and highly diversified farm. It looks nothing like the small homestead Bob started farming in 1968.

In the span of a generation, the push to produce more crops at lower costs has remade the business of farming. The median farm size in the United States is double what it was in the early 1980s, according to the U.S. Department of Agriculture, and farmers are responding by taking out larger loans to cover the added costs. More than 70 percent of farm loans are now over $100,000.

Today, the Merrills work 1,500 acres and employ several workers who aren't part of the family. They grow soybeans, corn and alfalfa in addition to milking 150 cows twice a day and raising 400 beef cattle.

Diversification is supposed to help farmers make it through tough years when the price of one crop plummets, but this year, just about every agricultural commodity price is low. Good weather around the world led to a flood of crops on the global market, driving down prices.

Farm Aid, an organization that tries to help family farms, has warned that America might be "on the cusp of the biggest wave of U.S. farm foreclosures since the 1980s." Farmers are currently carrying the highest level of debt since that crisis, when interest rates soared to the high double-digits and many family operations lost their farms.

"Another two or three percentage points higher on interest rates would be like a lightning bolt striking agriculture," said Jess Peterson, a Montana rancher and executive vice president of the United States Cattlemen's Association.

Loan lifelines

It got so bad for farmers in 1979 that thousands of them drove their tractors across the country at 15 mph to Washington, where they protested for weeks. Their first stop was Congress, but they later rumbled up to the Federal Reserve, where they picketed for lower interest rates, a shock to the central bank that normally receives little attention outside Wall Street.

Many farmers take out loans from local or regional banks. When farmers suffer, their local banks do, too. From 1984 to 1986, half of the 340 bank failures in the United States were agricultural banks that mainly worked with farmers.

Bob Merrill, Shane's grandpa, still blames the Fed for the 1980s panic. His voice changes as he talks about the grown men who cried in his kitchen before handing over their farm to the bank because they couldn't pay the interest on their loans. He's starting to see early signs that those days might be back.

The suicide rate among farmers has recently risen and is now the highest in any profession in the United States, according to the Centers for Disease Control and Prevention.

"Things are as hard as they've been for 20 years, maybe even since the 1980s," Bob Merrill said.

Tractors haven't yet shown up in Washington, but farmers and ranchers are starting to speak out to Fed officials.

In February, a top Federal Reserve official held a town hall meeting in Pierre, South Dakota's capital. These meetings are typically dominated by bankers who tend to favor higher interest rates. But this time, ranchers showed up, too.

Jason Frerichs, a 33-year-old rancher from Wilmot — a four-hour drive away — stood up at the town hall to urge Neel Kashkari, president of the Federal Reserve Bank of Minneapolis, to keep rates low.

"Average farmers just like myself will spend $20,000 to $50,000, $60,000 a year strictly in interest just to put our crop in the ground," Frerichs said.

Kashkari — one of the biggest proponents of keeping interest rates low among senior leaders at the Fed — told the ranchers not to worry because "we'll be in a reasonable interest rate environment well into the future."

That answer wasn't entirely satisfying to Frerichs, who works 9,000 acres with his father and brothers and is also a South Dakota state senator. He doesn't think the Fed understands what's going on in U.S. farming communities and how its actions could whipsaw through them.

"Rising interest rates put the family farm model at risk," Frerichs said. He wrote an op-ed published in MarketWatch in March calling on the Fed to keep farmers in mind.

"Each year I renew an operating line of credit that allows me to pay my landlords upfront for cash rent," he wrote, and also "to prepay seed, fuel, fertilizer and equipment repairs."

He wrote about "extremely tight" margins that caused many farmers to operate at a loss last year.

"And it looks very similar this year," he said.

Watching the Fed

Interest rates are much lower now than they were in the 1980s, but the Fed's plans to raise rates come as there has been a rapid decline in crop prices. A bushel of corn sold for more than $8 in summer 2012. Now it sells for less than $4. Soybeans and dairy have similarly tumbled.

Crop prices sank further this spring as President Trump edged the United States and China close to a trade war. The Chinese responded with threats to put tariffs on many U.S. farm products.

Fed leaders are set to meet June 12-13 to decide whether to raise interest rates. By a closely watched metric, Wall Street traders and economists predict about an 85 percent chance that rates will rise this month. Another increase is expected in September or December, plus more next year.

The Fed says it is raising rates because the U.S. economy is doing so well. Unemployment is the lowest it's been since 2000, there are a record number of job openings around the country, and growth is picking up as consumers and businesses spend more.

Jerome H. Powell, head of the Fed, wants interest rates to get back to more normal levels after years of near-zero rates that were aimed at reviving the economy after the Great Recession.

But how fast to raise rates is a complex calculation for the central bank.

Savers and banks tend to benefit as rates rise, though anyone who borrows money tends to be worse off because he or she has to pay higher costs. Raising rates too quickly could also trigger a recession as farmers and other business owners go out of business or scale back spending.

Younger farmers are especially vulnerable because they tend not to have as much land in their names, so they have less to offer the bank as collateral.

"We are highly leveraged. My parents didn't help me get started. We are at a lot more risk than a farm that's been in the family for generations," said Laura Daniels, a 42-year-old dairy farmer in Cobb, Wis., who runs the Dairy Girl Network.

Although Daniels grew up in a farming family, she and her husband opened their own farm a little more than a decade ago. They have steadily expanded to 300 cows and bought more land, but they took on debt to do so.

She wants to patch up her barn and add fans in her maternity pen, but there's no money left for that now.

With milk prices so low, many dairy farmers have had to go back to the bank.

"The only thing you can do is borrow more money. And many times, it ends up being those short-term loans with high [interest] rates," Daniels said. If rates get too high, "my farming operation will not survive."

Kashkari, the Fed official, is sympathetic to their plight. He noted in an interview on Thursday that he "voted against all three rate increases last year."

But the central bank's responsibilities go beyond one group. It must use the tools at its disposal to keep prices stable and achieve maximum employment.

"We wouldn't be doing our jobs," he said, "if we ignore our dual mandate and say we'll keep interest rates low to try to make up for trade uncertainties or low commodity prices."

2409 Comments

Heather Long is an economics correspondent. Before joining The Washington Post, she was a senior economics reporter at CNN and a columnist and deputy editor at the Patriot-News in Harrisburg, Pa. She also worked at an investment firm in London. Follow @byHeatherLong