

Introduction to farm loans

Most farmers take out loans to run their operations. Loans are often as much a part of farming as the weather. Farm loans generally come in two types, based on the length of time of the loan and what the loan is used to purchase.

Operating loans are short-term loans to purchase inputs to produce a product, whether crops or livestock, that will be paid back when the product is sold. Most operating loans last the duration of the production cycle, frequently a single season.

Ownership loans are longer-term loans, generally more than 5 years and extending as long as 40 years, for the purchase of major assets like farmland. Ownership loans are similar to home mortgages, paying off over a longer period of time. Collateral on ownership loans is generally based on a loan to value ratio, which is the percentage of the value of the asset being purchased that is being borrowed. If the entire value of the asset is being borrowed, the bank will generally require additional collateral to cover the possibility of loss.

Sources of farm loans

There are three major sources of farm loans; private banks, private banks with an USDA guarantee, and USDA direct loans. Different banks have different levels of comfort with farm loans, and may have specialties within their farm loan portfolio. It is important to work with a banker who has deep understanding of the operation that you are borrowing for, and the current status of the industry.

If the farmer cannot qualify for a private loan from a bank, the bank may be able to get an FSA Guarantee. In this case, the bank is still the lender, but the USDA's Farm Service Agency (FSA) agrees to pay up to 90% of the principle of the loan to the bank if the borrower is unable to repay the loan. Note that this guarantee is for the bank, not the borrower, and that it means that the risk of the loan is great enough that the bank is unwilling to take the risk without the additional protection.

The following sections have more detailed information about Direct and Guaranteed Loans.