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Rural Banking Credits

The functions and obligations of the Chartered Banks

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During the past few years a widespread misconception has arisen in the West as to the nature of the obligations of the banks toward the agricultural community and also as to how these obligations have been fulfilled. Complaints by individual farmers of inability to obtain credit to which in a few cases they were entitled but in most cases they were not, have been seized upon by the press as a basis for severe criticism of the banks as a whole. So much is this the case that the general public has come to believe that the banks cater only for commercial business and are not organized to provide for the credit requirements of agriculture.

I therefore wish to avail myself of the opportunity afforded me by the Editor of The Guide to inform the farming community that the banks are carrying loans to farmers and ranchers in the three prairie provinces estimated in 1915 at $75,000,000. As the total number of farmers in these provinces is probably not over 150,000, it will readily be seen that these figures reflect a liberal policy of lending. And let me add that the aggregate amount loaned to farmers at any given moment is always limited only by the amount of acceptable farmers' business which may be offering.

Moreover, I wish to say, without any reservation or qualification, that there is no business viewed with greater favor by the banks in every part of Canada than that of credits with farmers of a good type. If this were not true, what would be the explanation for the hundreds of branch banks at points in the west at which practically the only business to be had is that of farmers?

There is not now—nor has there ever been except during rare occasions of world-wide money stringency—any shortage of rural credit in Canada. Too much credit, and particularly too much of the wrong kind of credit, is what the western farmers have suffered from during the long period of agricultural prosperity prior to 1912.

The ownership of the funds administered by the chartered banks is, in round figures for all Canada, as follows:

Shareholders	$ 226,000,000
Holders of Bank Notes	122,000,000
Depositors	1,460,000,000
	$1,808,000,000

It will be seen from this that over 80 per cent. of the banking funds of the country consists of moneys of depositors. It has been argued by a prominent western statesman that these deposits belong to the people and that therefore the people have a right to say how they shall be loaned. This is inaccurate. The deposits belong to some of the people, and the banks are in the position of trustees for the individuals to whom the deposits belong.

Now the first obligation of the banks towards their depositors, beyond any room for argument or question, is to lend their moneys safely.

Recognizing the above duty to their depositors as paramount, the obligation next in natural sequence—an obligation alike to depositors and the public, implied by the terms of their charters and of the Bank Act—is to employ the country's banking funds only in accordance with principles of banking recognized as sound having due regard for the credit needs of a new country.

The necessity for maintaining a substantial proportion of their assets in the shape of cash and quickly convertible investments is obvious. The remaining funds of a bank should be employed only in the production and distribution of commodities, and in no case loaned against fixed assets such as lands and buildings. (The lending of money against the last mentioned kind of property is the special function of land mortgage and investment companies.) It is important to state this principle before proceeding to consider the subject of rural banking credits.

Then the allocation of that portion of the funds of banks available for production and distribution must always be determined by competition—competition among banks for the best and safest business; and competition among those who need banking accommodation, to establish the merits of their claims to credit, on the score of a record of integrity, industry, intelligence, thrift, progressiveness, coupled with evidence of ability to repay. No man has a right to borrow from a bank merely because he needs money even for a legitimate purpose. The burden must always rest on the applicant for credit to first establish his claim thereto; and if his claim should be a really good one, the circumstances would indeed be extraordinary if his record did not suffice to make the fact clear. This is a consideration which is often lost sight of by farmers who complain of their inability to obtain bank credit.

A loan to a farmer who can be relied on to use it to improve his position, is a contribution to the general welfare. On the other hand, credit extended to an incompetent and indolent farmer who is doomed to go broke, involves an economic loss to the country even though the bank should succeed in getting repaid. It is therefore the positive duty of a bank to avoid knowingly extending credit to a farmer who will not use credit advantageously, no matter what security he could offer.

Credits to Grain Growers

The question, however, of first importance to farmers is: What does constitute a basis for credit to them? What considerations determine whether a farmer can get credit from a bank, and the amount?

One writer in The Guide recently attacked my suggestion that under conditions existing in the west, co-operative credit associations should be founded on a pooling of assets, and he argued that personal character is the proper basis for credit and that a pooling of assets would be destructive of the independence of the borrower. While, however, character: i.e., possession of the cardinal virtues of integrity, industry, etc., is a fundamental pre-requisite of credit, it is by no means by itself alone a sufficient basis for credit. Ability to repay is also an essential requirement. A bank in dispensing credit will wish to be satisfied that a prospective borrower possesses means of repayment sufficient in extent to meet any normal reverse due to providential causes, as, for example, in the case of a good farmer, a crop failure.

It is a legitimate function of a bank to lend farmers the money required to put in and take off a season's crop, but in order to warrant such credit a farmer's position should be such that with a normal crop the returns therefrom would be sufficient to enable him to provide for all his floating debts—bank loans, mortgage interest, implement notes, etc. Banks do not ask more than this provided the farmer's land and implement debts are not excessive in relation to the amount of his capital, although, strictly speaking, in order to be a really first-rate risk for credit a farmer's position should be such that even with a crop failure he would still have enough quick assets left—grain, livestock, etc.—to counterbalance his floating debts.

Take a concrete example. John Smith, a grain farmer, at the beginning of a season shows assets and liabilities as follows:—

ASSETS

Good accounts	$ 210
Grain for sale	660
Quick assets	870
Seed Grain	140
Implements	800
½ Section	3,000
Work horses	900
	$5,710

LIABILITIES

Owing to bank	$ 600
Mortgage interest	80
Implement notes due	110
Floating debts	790
Implement notes not yet due	200
Mortgage	1,000
Surplus	3,720
	$5,710

It will be observed that he has enough quick assets with which to clean up his floating debts; that his mortgage indebtedness is moderate; and that his horses and equipment are nearly all paid for.

Assuming him to be reputed a good worker, cultivating his land well and enjoying the confidence of his neighbors, in Manitoba and Alberta he would have no difficulty in getting from a bank the credit necessary for a new season's operations, say $600 or $700. (I omit reference to Saskatchewan for reasons which I will explain later.)

Then should he have a bad crop failure, he would be owing the bank $600 or $700 which it could not collect promptly without putting its customer out of business, and in actual experience this is a situation which has occurred in thousands of cases during the past few years. In such circumstances what should the bank do? What it must do as a matter of common sense and good business, if it is satisfied that the debtor is a type of man who will eventually succeed, is to take security for the old debt, and stake him for another crop. It can legally take security for the old debt but must lend the new money without security because the Bank Act will not permit a bank to make new loans against mortgage security.

Suppose, however, that he has a second successive crop failure; that the bank then discovers that its confidence in its customer has been misplaced, the poor results of the farm having been due partly to poor methods; that the borrower takes refuge behind the exemption laws, refuses to give security for the later loans, and transfers his land to his wife. The bank would simply have to face a sharp loss, as has happened in no end of cases.

Take another case. Thomas Jones' statement at the beginning of the season is as follows:—

ASSETS

Good accounts	$ 210
Grain for sale	400
Quick assets	610
Seed grain	140
Implements	800
½ Section	3,000
Work horses	900
	$5,450

LIABILITIES

Implement notes due	$ 110
Mortgage interest	80
Floating debts	190
Implement notes not yet due	200
Mortgage	1,000
Surplus	4,060
	$5,450

This man could stand a crop failure and still be nearly able to pay his floating debts. His claims to bank credit for all his needs would be distinctly good—his position being far above the average for a quarter-section man.

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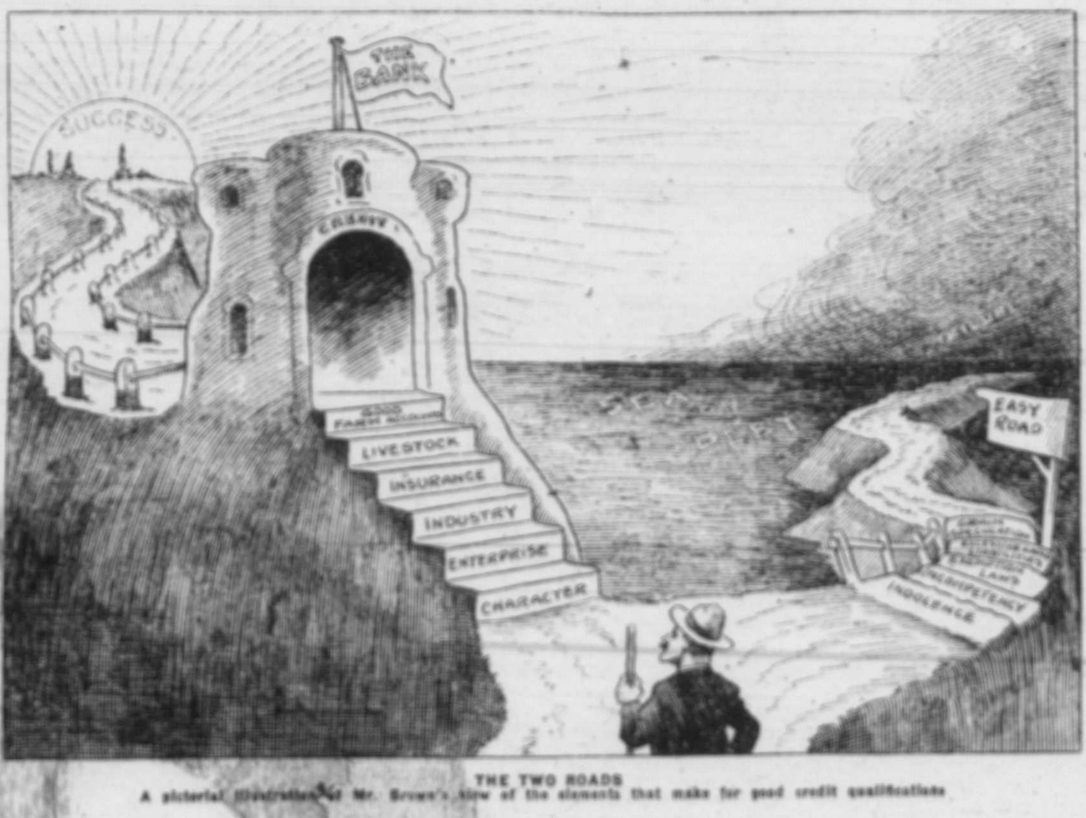

THE TWO ROADS
A pictorial illustration of Mr. Brown's view of the elements that make for good credit qualifications