Long-term debt reduces risk

AUSTRALIAN agricultural borrowers are far more reliant on variable and short-term fixed rate loans than their US counterparts and one agricultural lender says that trend can create an unnecessary risk.

About 86 per cent of Australian household borrowers sit on variable rate loans and the remainder typically fix their interest rates for three years or less, Foundation Agri Finance founder and executive director David Haydon said.

Agricultural lending follows a similar trend, with Australian farms heavily reliant on short-term, variable rate loans.

"This adds further volatility to a business model already exposed to variable seasons, production levels and commodity prices," Mr Haydon said.

"It also leaves business highly sensitive to changes in interest rates and to the prevailing appetite of lenders when they come to refinance their loan at maturity."

Mr Haydon said the situation was vastly different in the United States, where borrowers had a wider selection of lenders, and mortgages were taken out for longer periods, most commonly on fixed interest rates.

Only five per cent of household borrowers in the US sit on variable rate loans and the average fixed rate is 30 years, he said.

"Our observation from decades of working with agricultural businesses across Australia is that the most profitable farmers are the best managers of risk," Mr Haydon said.

"They take risk off the table to increase financial stability and generate higher, more consistent returns across the various cycles in agriculture."

An often underappreciated part of de-risking a business is managing refinancing-related risk and interest rate volatility, Mr Haydon said. "This is particularly important given the levels of debt in agriculture.

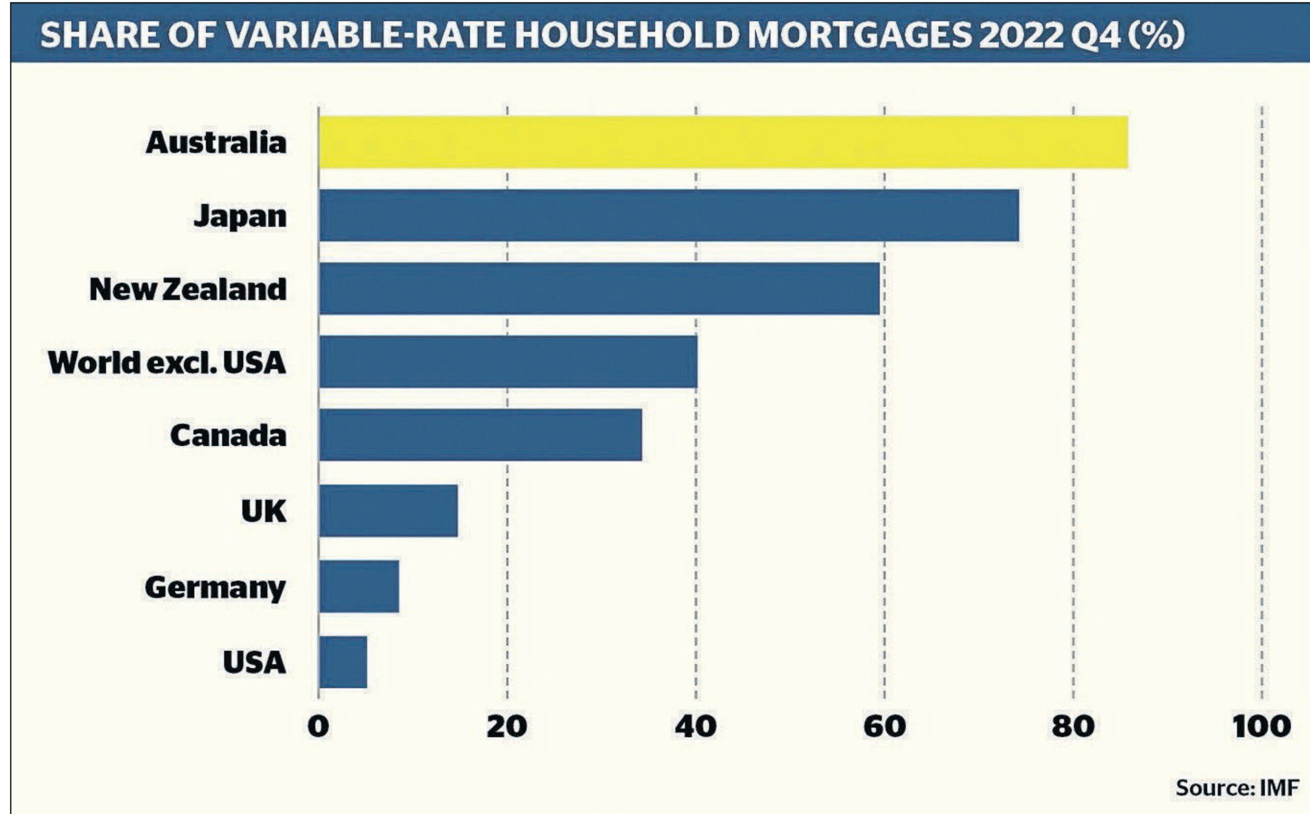
"Taking out longer loan terms and fixing rates on a portion of debt can be useful strategies to reduce risk."

He said agricultural businesses experienced large swings in profitability and these could be compounded by changes in interest rates.

"Early on in my career I was told debt was cheap until you needed it and the past few years has emphasised this," he said. "When things were going well, farmers had good access to debt at competitive rates. As it started getting drier and interest rates increased, it became harder and more expensive to secure debt to refinance existing loans and for new loans.

"Our cornerstone fixed-rate loan of up to 25 years provides farmers a different option to the short-term, variable bank loans and a way to lock in debt for the long-term."

This advice is general in nature. Readers are encouraged to seek professional advice.



Australia's heavy reliance on variable interest rate loans extends beyond housing markets to the agricultural sector.

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