

# Income, Wealth, and the Economic Well-Being of Farm Households

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## Introduction

Price and income support programs were implemented 70 years ago to provide financial assistance to farms, farm people, and rural areas. A key stimulus for legislative action was disparity between farm and non-farm incomes (Gardner, 1992; Houthakker, 1967). In fact, concern over this issue was reflected in references to “income parity” (U.S. Senate, Document No. 44). With some minimal adjustments, the price and income support system enacted then continues apace today.

Recent legislation indicates that Congress still holds a keen interest in farm income. As debate proceeded on the need for emergency assistance to offset low commodity prices in 2001, the discussion settled on “the viability of the American farmer and rancher and all of rural America” (Lancaster, 2001). Today, as with the transfer of income assistance broadly to farming through traditional commodity programs, little distinction is made between the status of farms and farm households. By treating the symptom of low commodity prices or flagging sectorwide incomes, it is assumed the problems of farms across the board are addressed. As evident in press accounts, another assumption is that addressing the income shortfall of farms will simultaneously resuscitate farm households (see “Defining Farm Households,” p. 2, for details) and rural areas.

When agricultural programs were devised, most farms were organized such that family members ran the farm, supplied most of the inputs, and earned the income. In today’s farming, a farm’s organization and operation are not so straightforward. Further, the continuing evolution of production agriculture raises a variety of issues to consider in developing policy for

modern farms and farm households. Is the farm problem, as many have argued, still defined by chronic low incomes? Are farm households inherently disadvantaged? Is income variation more problematic for farm households than nonfarm households? If so, what accounts for this and how do farm households adjust? If farm households have higher or lower incomes than nonfarm households, how do wealth levels compare?

## **An Evolution in Farming, An Evolution in Thinking**

Policy analysts, farm investors, and lenders are among those interested in monitoring and forecasting the economic well-being of the farm sector and farm households. Historically, attention has focused on farm incomes. But since farming today is only one of several economic endeavors of farm households, household income is more indicative of an individual’s welfare. A meaningful comparison among farm households and between farm and nonfarm households must also include a measure of wealth (Hill, 2000). Hill points out that wealth is important not only because it generates income in a variety of forms but also because it provides security, freedom to maneuver resources, and economic and political power. Wealth is an often neglected but important determinant of the financial status of farms and rural communities.

Estimates of personal income for the U.S. farm population date to 1934 and the first available data on the nonfarm income of farm people. While this income measure was for a subset of the farm population, it provided a basis on which to compare farm and non-farm incomes. Between the 1930s and 1960s, estimates of personal income showed nonfarm income of farm residents rising as a proportion of total income. Randall and Musucci (1963) noted changes in farm

## Defining Farm Households

The households of primary operators of farms can be organized as individual operations, partnerships, and family corporations. These farms are closely held (legally controlled) by their operator and the operator's household. Farm operator households exclude households associated with farms organized as nonfamily corporations or cooperatives, as well as households where the operator is a hired manager. Household members include all persons dependent on the household for financial support, whether they live in the household or not. Students away at school, for example, are counted as household members if they are dependents.

structure and occupation that raised questions about the use of farm population income estimates. Specifically, farm operators and hired workers were moving to town, which, in addition to rural migration, increased the number of rural residents who did not depend on agriculture as a primary occupation. To address these concerns, estimates of income for operator families gained prominence and two major groups of farms emerged (Randall and Musucci, 1963). More commercially oriented farms derived the majority of their income from farming. A second group, accounting for 60 percent of farms, earned most of their income from off-farm sources.

During the 1970s and 1980s, several researchers noted changes in the composition of farm family income (Larson and Carlin, 1974; Hanson and Spitze, 1974; Carlin, 1973; Reinsel, 1974; Larson, 1974; Crecink, 1979). While these studies drew from a wide variety of data, they all noted the improvement of farm household income relative to the incomes of nonfarm households. Instrumental in closing this gap was income from off-farm employment. Larson and Carlin argued that farm income was no longer a reliable barometer of the welfare of farm people. Changed economic conditions in the farm sector often translated into very minor changes in the money incomes of farm households. Reinsel posited substantial differences among households within the farming sector, while Hanson and Spitze uncovered the significant contribution of operators' spouses to household income through their off-farm employment. Off-farm work by farm families has been examined from the perspective of part-time farming and as an employment choice that extends across types and sizes of farms. Allocating labor to both farm and nonfarm activities enables farmers to increase income and raise levels of satisfaction; such a choice does not, by itself, indicate anything about the productivity of the farm (Lee, 1965; Bollman, 1979; Singh and Williamson, 1981).

Generally, part-time farming has been presented as the two-fold occupation of the farm operator (Singh and Williamson, 1981). Dual employment has referred to farm families combining farming activities with off-farm employment (Huffman, 1991; Hanson and Spitze, 1974; Ahearn and Lee, 1991). On some farms, the operator may continue to farm full time while household members take off-farm jobs. On other farms, the primary operator may be the person principally employed in off-farm work. For other farms, both the operator and other household members may choose to combine farm and off-farm work, becoming in effect both part-time and dual-employment operations.

A variety of individual, family, and farm/financial characteristics—as well as local labor markets—affect farm labor choices. Influencing the allocation of labor are age, size of family, size and type of farm, location and employment characteristics of nonfarm labor markets, skills and experiences of household members, and costs of commuting (Huffman, 1991; Sumner, 1982; Lass et al., 1989; Gunter and McNamara, 1990; Huffman and El-Osta, 1997; Mishra and Goodwin, 1997; Kimhi, 2000).

Patterns of income and wealth associated with the life cycle have been examined for differences among age groups of farmers (Ahearn et al., 1993). An inverted-U shape emerges in the age-earning profile for farm operators, whereas net worth is either fairly flat or rises with age to a plateau. This combination tends to overstate (exaggerate) asset values in relation to incomes in the latter stages of life, affirming the adage of live poor/die rich. The high-wealth low-income combination, found particularly among elderly farmers, should draw attention to wealth's role in the assessment of economic status and the criteria for public support. This rethinking may suggest ways in which households can enhance current spending power, avoiding the transfer of income from other sec-

tors of the economy as mandated by traditional policy mechanisms.

To move beyond a single dimension of well-being, measures that consider both income and wealth have been advanced (Weisbrod and Hansen, 1968). Both current income and current net worth are important determinants of a household's economic position (with an economic unit's well-being as a function of the flow of services that it can command). Salant et al. (1986) used this type of approach to build viability ratios for farm households. They defined a viable household as one that generated enough net returns from all sources to cover family expenses, repay debt, and replace capital that has been used up. Other researchers (Bauman, 1999; Smith and Morgan 1970) have introduced consumption into the notion of economic well-being, which can change either due to change in the level of income or to adjustments in family consumption needs.

While the importance of off-farm work in improving household incomes has long been a matter of record, income analyses have typically overlooked variations in source, except for noting whether income was earned by the operator, spouse, or other family member. An exception is a line of research that decomposes the distribution of income among farm households by

income source (see Ahearn et al., 1993; Findeis and Reddy, 1987; Boisvert and Ranney, 1990; and El-Osta et al., 1995). These articles looked at the cross-sectional variation in total household income in terms of the importance of income from farm (including government payments) and off-farm sources. While these studies examined the extent of variation in total household income attributable to the farm and off-farm income source, they did not look at income variability over time.

This report fills that void by examining variability in total household income over time by sources of income. To do so, we explicitly examine farm and off-farm sources of income, particularly whether off-farm incomes are derived from earned or unearned sources. Earned sources are either wage/salary or self-employment for both operators and spouses. Farm income, wealth, and consumption are joined to yield an explicit consideration of household well-being. We subsequently demonstrate how perceptions of farm households' well-being that are based solely on income can be significantly altered when wealth and consumption are introduced. The report also examines how the economic status and well-being of farm households compare across groups of farms and farm families and with all U.S. households generally.