

Top of Mind

In a recent interview, a reporter asked me what was “top of mind” for agricultural lenders, producers and agribusinesses across the country. Well, some obvious macro factors such as, the new Administration, commodity markets, and now interest rates are common themes. However, there are some specific concerns for the bottom line.

One topic that is top of mind for many lenders is the quality and timeliness of financial reporting. According to several lenders, the quality of financial information waned during the great commodity super cycle from 2008 to 2013. Now, balance sheets often lack full disclosure of accounts payable and capital leases such as, tractors and combines. In assessing livestock numbers and grain bins, the number of on-farm inspections continues to increase. This, of course, takes a considerable amount of time and effort piled upon already heavy-laden inspection workloads. Producers will have to accept the fact that increased transparency including more serial numbers and livestock identification is the product of our times. For many in the agribusiness sector, revenues are also down. It is reasonable to expect agribusinesses to closely monitor accounts payable, operating lines and pledges of security as collateral.

The reality for lenders is that agriculture is in a period of debt restructure and refinancing as a result of the economic cycle. The concern is whether the restructures present acceptable risk for the lending institution. In some cases, it may be best for the customer to consider an exit from the business. As a producer, expect your lender to calculate burn rates not only on working capital, but on core and land equity in order to determine the resiliency and agility of the business.

Another concern of agricultural lenders and institutions is the drain on human capital especially amongst the senior staff. Of course, the economic reset is taking an emotional toll on agribusinesses and producers as well. In order to be a successful lender in today’s environment one must quickly grasp a producer’s financial situation, the current state of the industry, and the method of communication best suited for a particular customer, all in a stressful situation. Lenders must balance their concern for their customers as well as the additional regulation and scrutiny. Good training and experienced mentors are both strategies many lenders have already begun to employ.

Finally, lenders are assessing management skills and quality. The financial farm record systems are clearly highlighting management as the “sixth C,” as fittingly named by former First Dakota Executive, Denny Everson. In other words, in today’s economic environment the differences between profit and loss are management skills, not production yield or current price. Of course, management touches every detail of a farm business, but there are specific areas really showing up as the difference makers. Knowing the cost of production, executing a marketing and risk management, having a firm grasp on financials, and valuing and energizing the human component are some of the management elements markedly affecting the bottom line.

In order to make profits in this economic environment, producers must be proactive. They need to seek information and guidance on methods of improvement. Even just small adjustments applied over several areas of the business can significantly drive efficiency. Many producers have accepted the fact that the time period of 2008 to 2013 was an economic aberration. Actually, that situation has only been seen three other times in the past one hundred years. By contrast, reactive producers are ignoring economic realities and may soon find their businesses beyond repair. One producer succinctly described today's producers in three categories: vulnerable, in recovery with some high-risk, or resilient and agile.

Cash flow budgets are a good way to determine whether cost of production is being covered. Most of the farm businesses in the vulnerable category are not covering variable costs and have not been covering them for some time. In business and economics, this is a sign that drastic action is needed or the business should be dissolved.

Interestingly, some of those in the resilient and agile category are considering additional land purchases or business expansion. Others are taking the "wait-and-see" approach allowing land values to decline, while others only seek high-quality lands in close proximity to their existing operations.

Another topic that is top of mind for other producers is liquidity. In order to increase financial liquidity, some producers are selling land and farm assets. This extra cash may be the bridge for an extended downturn, or a launch pad to grow the business in coming years.

Similar to 1980s, lenders are using the economic downturn to strengthen relationships and work closely with producers to improve financial margins. Although the specifics vary, finances are top of mind for all sectors of agriculture, including production, agribusiness and lending. Producers and businesses that are willing to adapt, strategize, execute and implement change have a much greater chance of success. Along with their lender, producers that monitor business performance will remain in control of their economics instead of economics controlling their business.

Management Tip:

Our team at Homestead creamery had the opportunity to hear future Hall of Famer, Peyton Manning speak recently. He said, "You have to be coachable." Regardless of whether you are a business owner, manager, lender, or agribusiness professional, being open-minded to change is the key to success.