Viewpoints from the Road

"On the Road Again" by Willie Nelson would be an appropriate song for this summer's travel season. Producer seminars, banking conferences, and schools provided a vantage point of engagement with individuals across all walks of life. Here are some of the viewpoints from this summer's travels.

The television interview

A television station in Fargo, North Dakota, invited yours truly on a live program. The newscaster asked a very pointed question, "According to individuals in his district, Minnesota Congressman Collin Peterson recently stated that agriculture is headed for a crisis worse than the 1980s. Any comments?"

Congressman Peterson has some credence in his view. Agriculture is in the midst of a seven-year economic downturn which is impacting profits, cash flow, and liquidity. Fortunately, the collapse of land values has not occurred in many areas of the country. Farmland represents 83 percent of the U.S. farm balance sheet, which provides resilience to many farmers and ranchers. A steep correction in land values would bring the agriculture industry to its financial knees.

Over the next 12 months, watch for the appetite of both lenders and producers to use equity to stretch out operating losses over 10 to 20 years. Next, keep a close watch on interest rates. Low interest rates provide greater flexibility and allow producers to lock in favorable terms when refinancing. Also, continue to monitor the appetite of outside investors willing to purchase land placed on the market. When it comes to land values, only time will tell, and we could see reductions in asset values occurring in select areas of the country.

How does the bank of mom and dad fail?

An increasing number of young and beginning farmers and ranchers are obtaining their loans from the bank of mom and dad or extended family. Farms that are in financial stress frequently reach out to family members to bridge the financial gap. When and why do these private financing agreements fail?

First, these agreements fail due to a lack of accountability. Private financing agreements are often settled with a handshake or nod and are very emotionally driven decisions. While the willingness to provide financing is admirable, a written and defined payment plan needs to be developed and executed even with family members. In the event of financial adversity, many times private financiers are willing to delay payments or, in some cases, forgive debt. In other cases, the older generation has lost equity in their golden years as a result of assisting family members and not knowing the true financial picture.

If the younger generation is required to seek financing with a traditional lender, then they can build a credit reputation to leverage for future growth and expansion. My overall advice for private financing would be to document the agreement in writing and verify the borrower's situation before extending credit to family members.

Agriculture balance of export power

While the trade wars have been front and center for the agriculture industry in recent years, a longer-term view may provide some interesting perspectives. Let's go back to the decade of the 1970s when the U.S. corn export market share was 75 percent; this has declined to 64 percent by 2001. Currently, the U.S. corn export market share is approximately one third of the export market. What countries have increased their corn export market share? Argentina was a player in the early 2000s at 12 percent market share and Brazil came in around 8 percent. Today, Argentina and Brazil collectively represent nearly 40 percent of the corn export market share with Brazil picking up steam.

Moving to soybeans, a more dramatic loss in U.S. export market share can be observed. In the 1970s, the U.S. had 96 percent of the soybean export market share. The U.S. soybean export market share has since declined to 50 percent by 2001 with Brazil and Argentina knocking on the door at a combined 40 percent. Today, the soybean export market share is 35 percent for the U.S., 50 percent for Brazil, and four percent for Argentina.

Five factors are impacting these trade changes. Technology, new land in production, weather and climate change, and improvements in infrastructure in these countries have had a major impact. The acceptance of the Chinese currency in exchange between these countries is also accelerating change. Interestingly enough, other commodities are experiencing some declines in market share as trading partners seek alternative sources of food, fiber, and fuel. This places pressure on commodity prices here in the U.S. and throughout the world.

60/30/10 Rule becomes 10/60/30

The 60/30/10 rule could quickly describe the macro-economic status of the commodity super cycle from 2003 to 2012. Sixty percent of producers were "hitting economic home runs" and observing record profits. Thirty percent of producers operated in the black with base hits concerning profits while 10 percent lost money and were operating in the red. Since 2013, these quick measures of profitability can be flip-flopped. Ten percent of producers are hitting home runs and generating financial profits, often by capitalizing on value-added markets or side gigs aligned to the marketplace. Sixty percent of producers are operating with modest profits, while 30 percent have been losing money. The bottom line is that the winning formula for operating profitably during this economic cycle is with a game plan of base hits. The ten percent of profitable producers know their numbers and are usually good at marketing and risk management. They also prioritize capital and human resource efficiency.

Where are we in the economic cycle?

An agriculture producer recently asked me the following question, “In 2015 at a national conference in St. Louis, you mentioned that we were in the infancy of a five to seven-year winter cycle in agriculture. You also recommended to zero in on the financials, marketing, and efficiency of our operations and to cautiously expand. Do we have two more years left in the winter cycle?”

When considering the grain market, the down cycle will continue unless broken by a weather event that may provide a temporary boost in commodity prices. On the livestock side, the African swine fever or other similar events could provide a rise in prices. Longer-term technology and consumer trends will not only impact commodity prices, but those engaged in value-added businesses.

P.S.
It was creepy when lecturing at the Graduate School of Banking at Colorado how other speakers indicated that hemp was going to be the “billion-dollar savior” of U.S. agriculture. Another instructor informed me that he was in love with the plant-based burger because it was “saving the environment.” My only comment to the respective speakers was that there is no magic silver bullet for profits and that buffalo numbered 30 million a number of years ago and passed gas for centuries! Maybe these individuals enjoyed some special brownies while in Colorado!