

# *POSITIONING FOR SUCCESS IN CYCLICAL ECONOMICS*

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Macro Clinic Video Blog: [www.compeer.com/education](http://www.compeer.com/education)

Road Warrior of Agriculture: [www.cornandsoybeandigest.com](http://www.cornandsoybeandigest.com)

Ag Globe Trotter: [www.northwestfcs.com](http://www.northwestfcs.com)

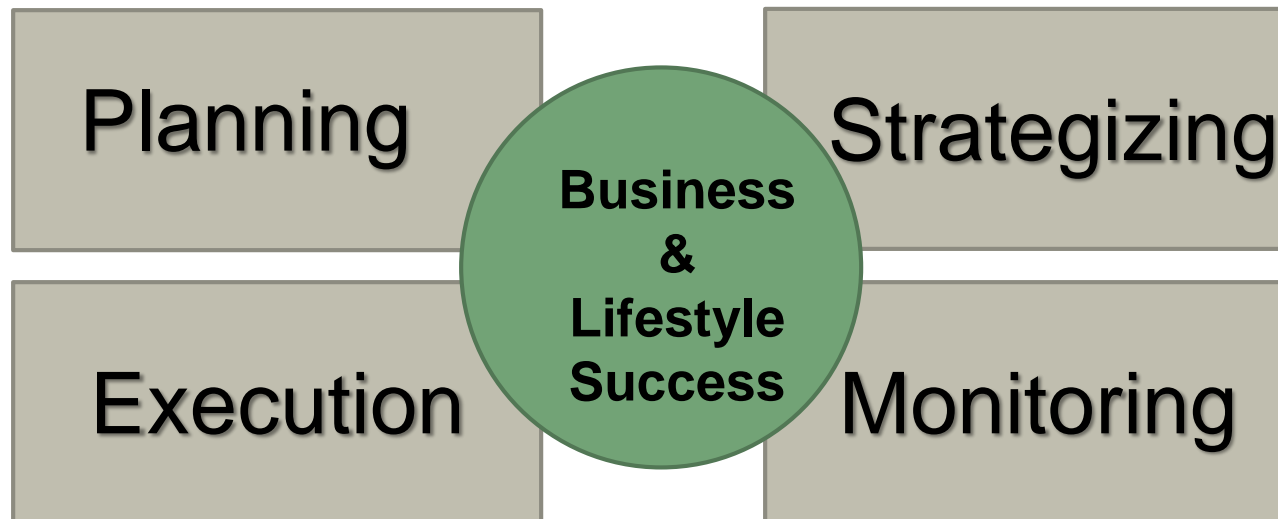
Dave's GPS & Dashboard Indicators: [www.farmermac.com](http://www.farmermac.com)

# Views from the Road

- agriculture is in the 7<sup>th</sup> year of economic reset
- dairy is in the 4<sup>th</sup> year of economic reset
- low margins, high volatility
- manage with focus & manage around the noise or uncontrollables
- Business IQ will be the difference maker
- grinder- financial and emotional toll

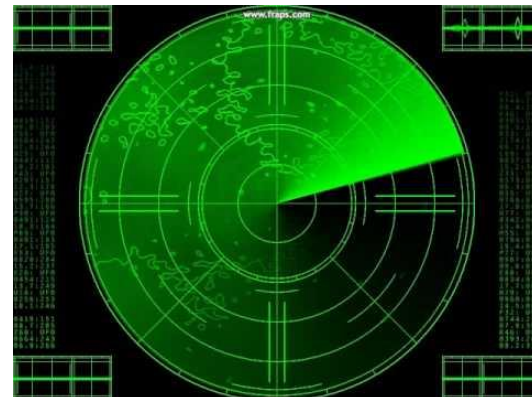


# *Four Cornerstones of Management*



# *Economic Radar Screen*

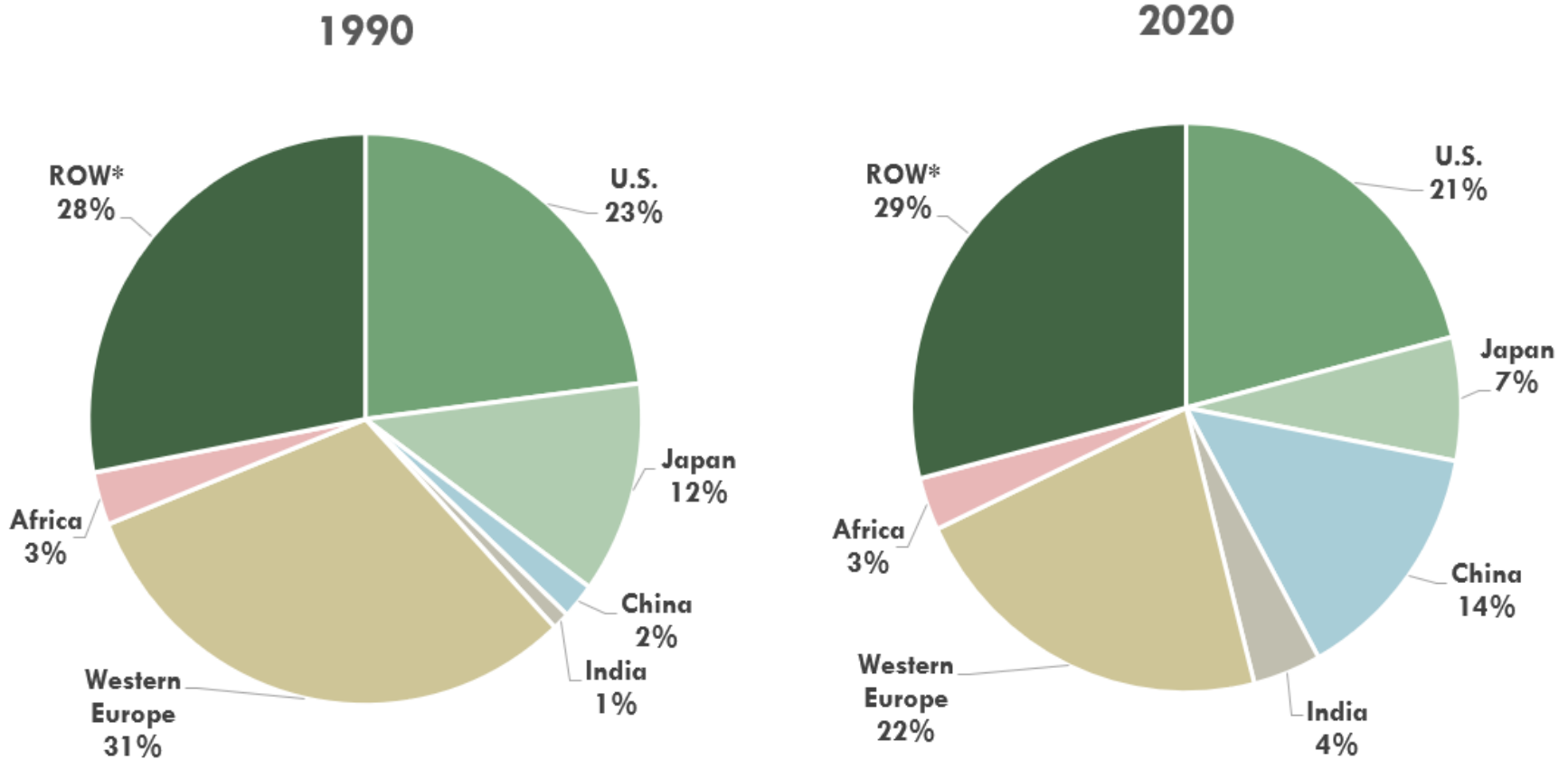
- international trade
  - USMCA
  - China's Belt & Road Initiative
- synchronized global economic slowdown
  - China- slowest growth rate in 28 years
  - Japan- negative growth rate
  - Germany – negative growth rate
  - Central Bank's stimulus in China
  - high debt levels in urban real estate in China
- political uncertainty
  - Brazil
  - Venezuela
  - Mexico
  - Argentina
  - Germany, Britain & Euro Sector
  - U.S.



# *North America's Economic Power Block*

- 28% of the global economy's GDP
- energy & oil
  - U.S. #1
  - Canada #4
  - Mexico #8
- 450+ million people
- 47% of Mexico's population is under 25
- ag trading partners:
  - Canada #1
  - Mexico #3

# Rising of Asia



\* ROW- Rest of World

Source: Global Insights, August 2018

# *Farm Real Estate Perspectives*

- farm real estate appreciated or stayed level 79% of years from 1910-2017
- since WWII (1941) farm real estate appreciated or stayed level 88% of the years
- 1910-WWII (1940) farm real estate appreciated 57% of the years
- farm real estate was flat or declined for 13 years from 1920-1933
- farm real estate declined for four years in the 1980's

# *Drivers of Change on Land Values*

- interest rates
- investor funds
- refinancing cycle
- baby boomer farmer
- relatives who inherit land
- supply and demand of commodities
- crop insurance





# *State of U.S. Economy*

- 110-plus months
- 106 & 120 months
- urban and coastal economies and the fly over states
- central bank driven- U.S. and abroad
- wealth effect
  - consumer investing
  - consumer spending

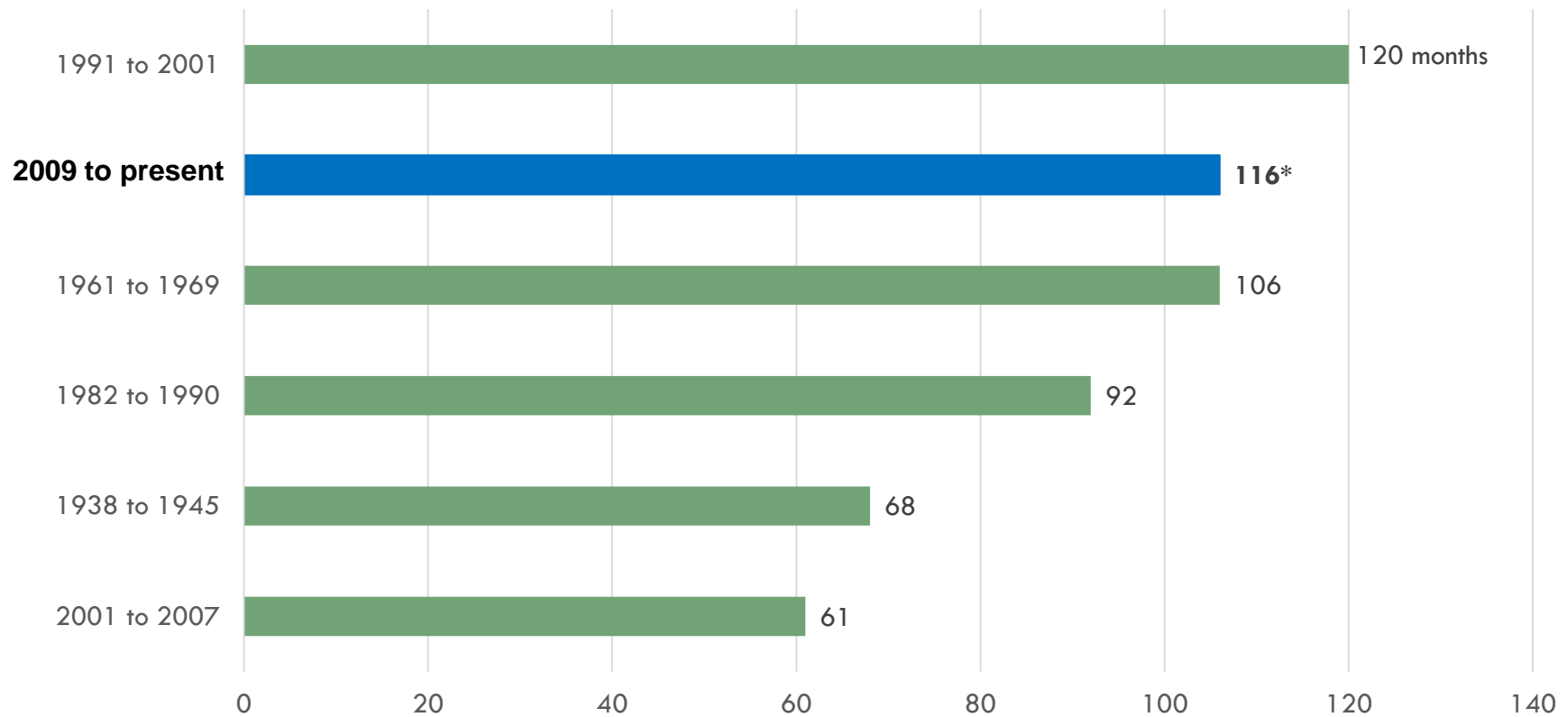


**IMPACT: killers of economic expansions**

# By Mid-June, Longest Economic Expansion in the U.S.

## Longest economic expansions in modern U.S. history

(As of February 2019)



Source: NBER, Economic Cycle Research Institute (Note: current expansion still in progress)

# Federal Reserve's Interest Rate Barometer

- two rate increases in 2019
- one possible rate decline in 2019

| Indicator          | Current Estimated<br>“Flag” Levels |
|--------------------|------------------------------------|
| Unemployment       | Below 5.0% or<br>Above 6.0%        |
| GDP Growth         | Above 3.0% or<br>Below 2.0%        |
| Inflation          | Above 2.5% or<br>Below 1.0%        |
| Consumer Sentiment | Above 90 or<br>Below 80            |

- trends matter
- stock market/real estate wealth effect
- copper prices

# *Mega Trends 2020-2030: “High Beams”*



# *Mega Trends 2020-2030: Dietary Trends*



- Millennials, Gen Z & Baby Boomers
- cultured meat & non-dairy
- vegans- U.S. & abroad
- environmental footprint
- 95% of success is alignment of:
  - resources
  - talents
  - markets
- experiences & personalization vs. commoditization

***“We have not seen anything yet.”***



# Mega Trends 2020-2030: Technology/Consumer



- bio engineering
- information convergence
- production
- consumers/food industry/producers
- great wall of protein & “impossible burger sliders”
- skill base
  - analyze data
  - critical thinking
  - communication
- first replaces labor
  - higher level of talent
- systems/replicate – use of information data
- too connected

***“Think beer.”***



# *Mega Trends 2020-2030: Tech Transformation*



- robotics
- data in the food chain
- retail & wholesale disruption
- blockchain technology

*“Market disruptors.”*



# Mega Trends: Technology & Production



Metric Tons Increase Since 2008-2009 til 2018

| Country   | Corn<br>(Percent Change) | Soybeans<br>(Percent Change) |
|-----------|--------------------------|------------------------------|
| U.S.      | 21%                      | 55%                          |
| China     | 48%                      | 1.1%                         |
| Brazil    | 85%                      | 108%                         |
| Argentina | 174%                     | 73%                          |
| Canada    | 36%                      | 125%                         |
| Europe    | -9%                      |                              |
| Paraguay  |                          | 168%                         |

Source: Kirksville, MO presentation - University of Missouri





# *Mega Trends 2020-2030: Non-Government Organizations*



- Smithfield lawsuits
- Monsanto lawsuits
- others
- biosecurity
- open pens
- antibiotic free
- animal welfare

***“NGOs more disruptive than  
government regulations.”***



# *Mega Trends 2020-2030: 2020 Decade of Transition*



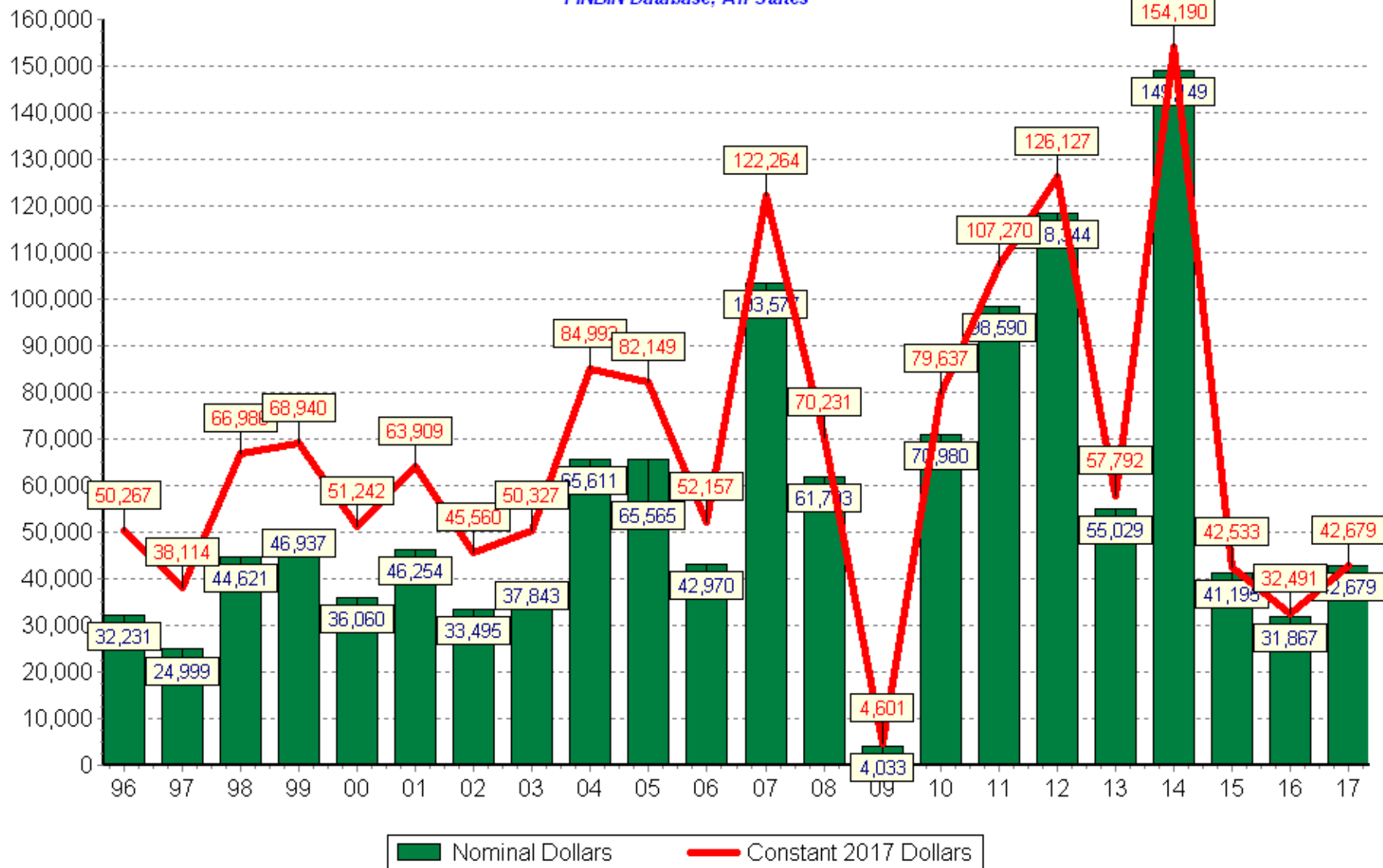
- agri-entrepreneurs multi task
- larger complex businesses
  - cousins
  - non-family members
- women in farming, ranching, ag lending, and agribusinesses
- ag lending / non-traditional

***“The mythical becomes typical.”***



# Median Net Farm Income - Dairy Farms

FINBIN Database, All States

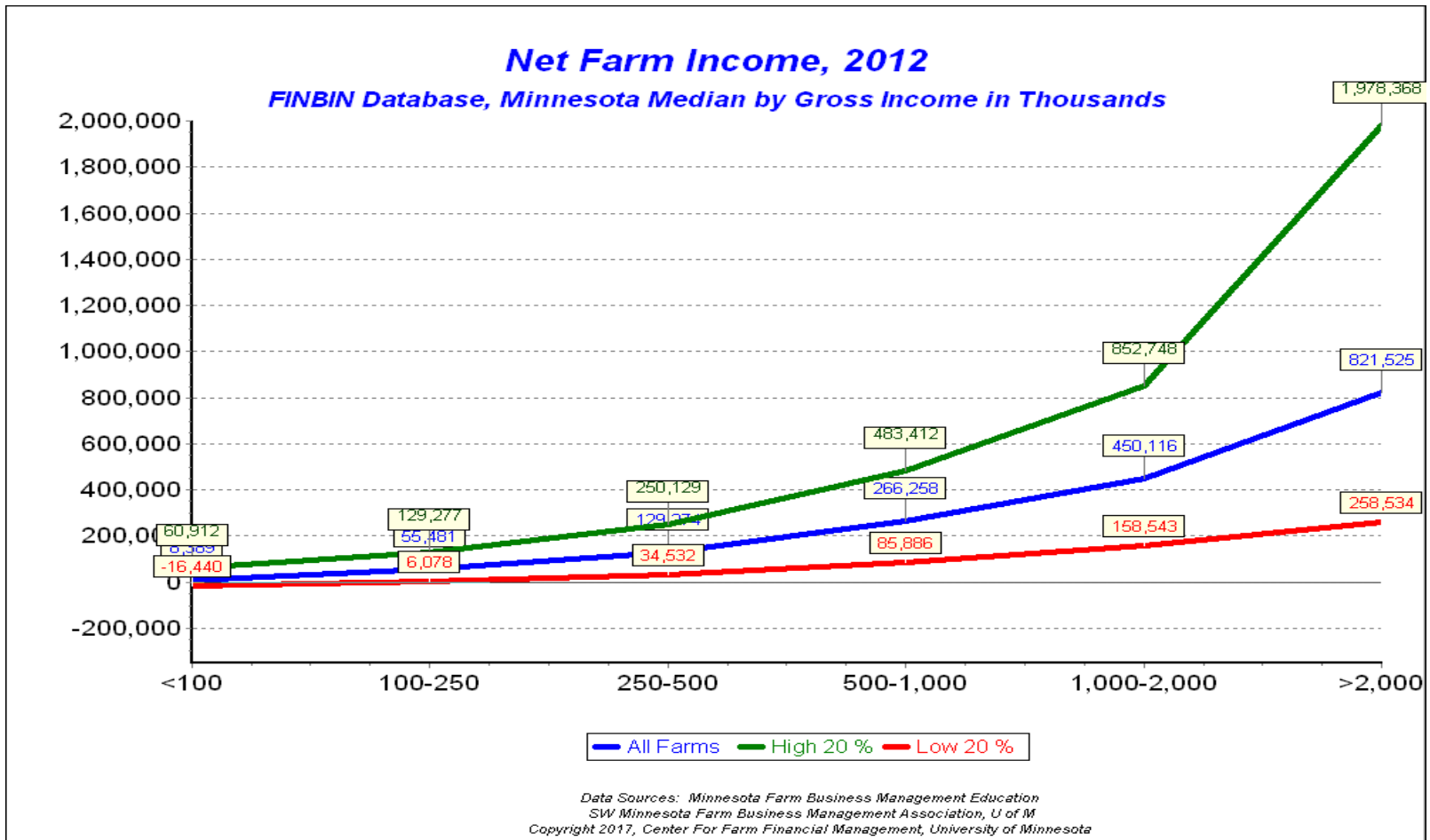


# *Producer Concerns*

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- interest rate increase impacting cost of production
- family living expenses leveling off- too many generations of people living out of the business
- off farm employment and health benefits
- cash flow profits
- working capital
- land equity drain
- income, labor, and input costs

# Net Farm Income, 2012



# Net Farm Income, 2016

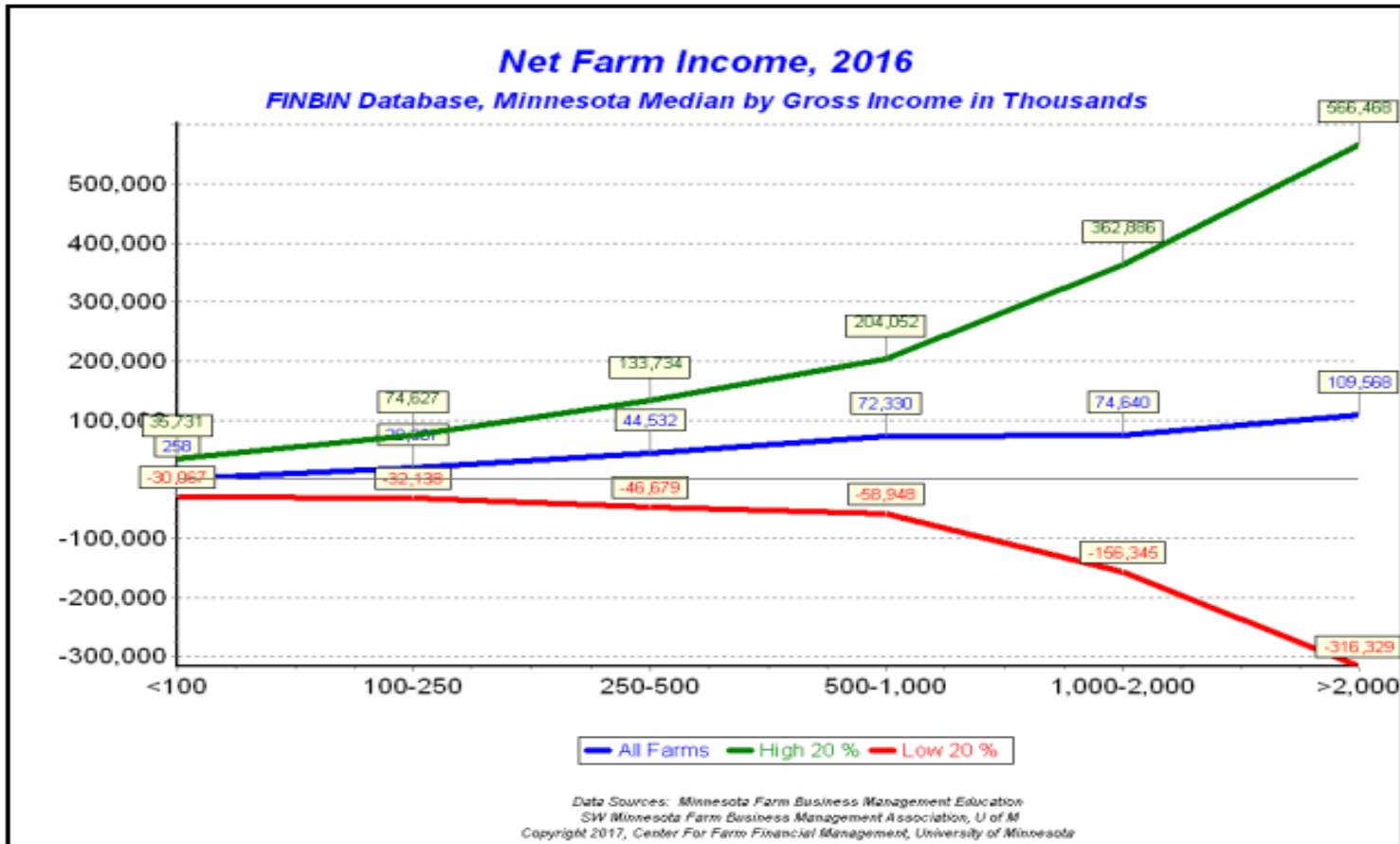
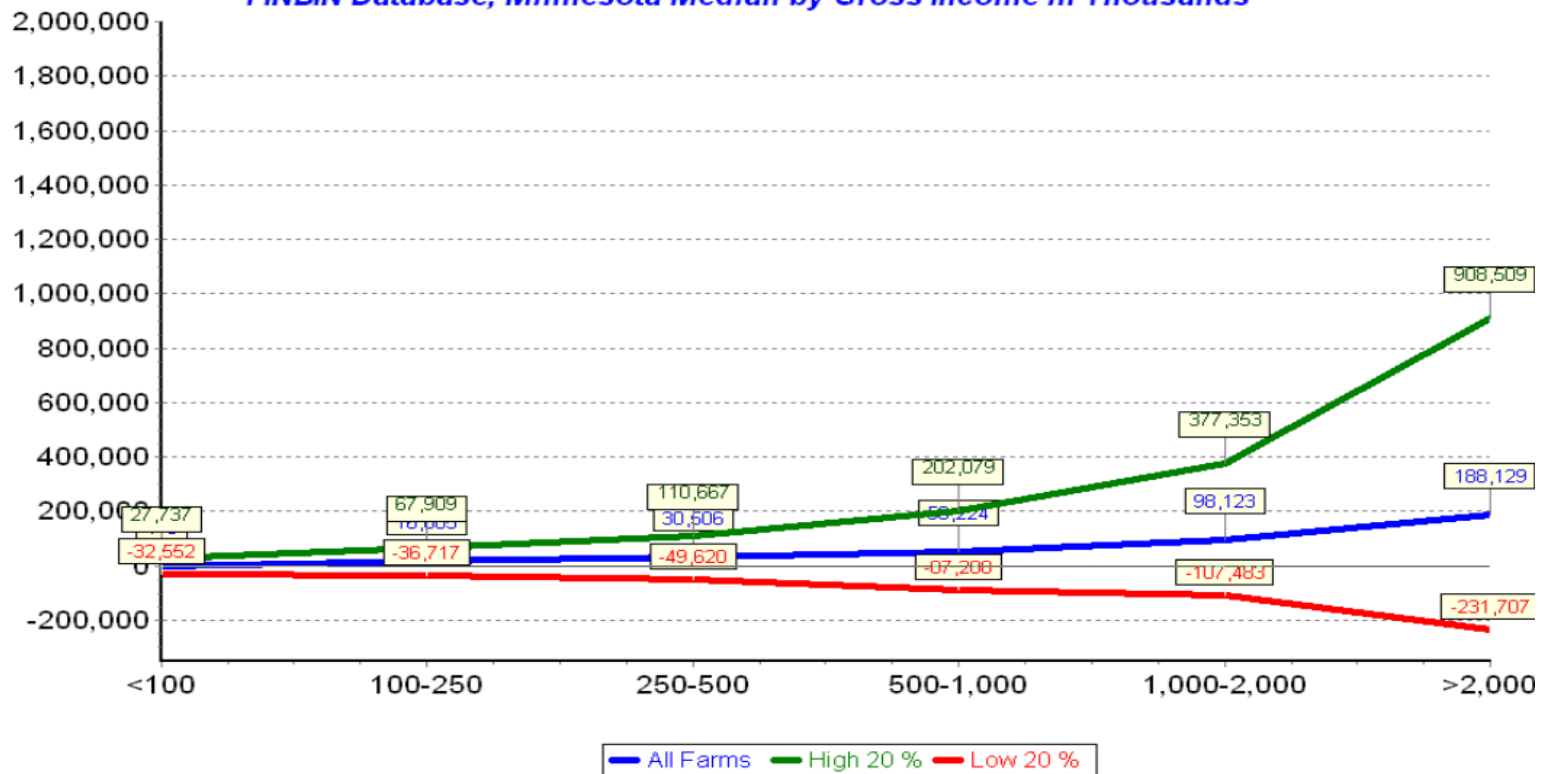


Figure 13: Net Farm Income by Farm Size

# Net Farm Income, 2017

## Net Farm Income, 2017

FINBIN Database, Minnesota Median by Gross Income in Thousands



Data Sources: Minnesota Farm Business Management Education  
 SW Minnesota Farm Business Management Association, U of M  
 Copyright 2018, Center For Farm Financial Management, University of Minnesota

# *Why Some Businesses Are More Profitable Than Others*

- These businesses are a “**little**” better at:
  - production
  - marketing
  - cost control
  - asset and capital efficiency
- utilize the 5% Rule



# Business IQ: Management Factors

## Critical Questions for Crucial Conversations

| Customer Checklist   | Green (3-4 points*) | Yellow (2 points)       | Red (1 point)            |
|--|---------------------|-------------------------|--------------------------|
| 1. Knows cost of production  | Written             | In head                 | No idea                  |
| 2. Knows cost of production by enterprise                            | Written             | In head                 | No idea                  |
| 3. Goals- business, family & personal                                | Written             | In head                 | No idea                  |
| 4. Record keeping system   | Accrual             | Schedule F (one & done) | No idea                  |
| 5. Projected cash flow   | Written             | In head                 | No idea                  |
| 6. Sensitivity analysis  | Written             | In head                 | No idea                  |
| 7. Understand financial ratios, break evens                          | Written             | In head                 | No idea                  |
| 8. Work with advisory team and lender                                | Yes                 | Sometimes               | Never                    |
| 9. Marketing plan written and executed                               | Yes                 | Sometimes               | Never                    |
| 10. Risk management plan executed                                    | Yes                 | Sometimes               | Never                    |
| 11. Modest lifestyle habits, family living budget                    | Yes                 | Sometimes               | Non existent             |
| 12. Written plan for improvement executed & strong people management | Yes                 | Sometimes               | Non existent             |
| 13. Transition plan/Business Owner plan                              | Yes                 | Working on plan         | Non existent/controversy |
| 14. Educational seminars/courses                                     | Yes                 | Sometimes               | Never attend             |
| 15. Attitude   | Proactive           | Reactive                | Indifferent              |

### \*Extra Points:

- **Progressive Business** may receive 4 points for #2,6,7,8,14
- **Struggling Business attempting turnaround** may receive 4 points for #3,5,8,11,12

| Score | Overall Analysis  |
|-------|---|
| 35-50 | Strong management rating & viability                                  |
| 20-34 | Moderate risk & viability; will most likely show previous refinancing |
| <20   | High risk & lack of long term viability                               |

# ***Trouble Shooting Matrix***

## **Insufficient Repayment Capacity**

**Cut Business Cost**

Reduce Four Largest Expenses: Crop, Feed, Labor, ??

**Non-Farm Revenue**

Job Stability/Availability, Job Cost  
Job Earnings, Skills, Time Management

**Increase Income**

Sell Capital Assets, Deferred Taxes,  
Increase Production, Increase Price

**Cut Living Withdrawals**

Purchase Financial Software, Small Cost Containment

**Restructure Debt**

Longer Term, Interest Only,  
Principal/Interest Deferred

**Capital Infusion**

Equity Capital, Family Capital,  
Supplemental Cash Flow

**Bankruptcy**

Voluntary, Involuntary,  
Chapter 7, 11, 12, 13

# Character Counts

## Critical Questions & Observations for Customers

| Customer Checklist   | Yes | No |
|--|-----|----|
| 1. Are they honest, ethical & trustworthy?   |     |    |
| 2. Do they report all assets & liabilities accurately?                             |     |    |
| 3. Do they use borrowed funds as agreed upon?                                      |     |    |
| 4. Have they managed through adversity?  |     |    |
| 5. Have they followed through on educational opportunities?                        |     |    |
| 6. Have they saved for lifestyle pursuits & balance with business growth?          |     |    |
| 7. Have they had minimal surprise purchases & not obtaining credit after the fact? |     |    |
| 8. Have they used profits and windfalls properly for cashflow?                     |     |    |
| 9. Have they been willing to work with advisory team?                              |     |    |
| 10. Have they considered coaching and constructive advice?                         |     |    |
| <b>Totals</b>  |     |    |

| Total Yes        | Character Assessment |
|------------------|----------------------|
| 8-10 Yes Answers | Strong               |
| 4-7 Yes Answers  | Fair                 |
| <4 Yes Answers   | Weak                 |

# Critical Financial Performance Index for Debt & Risk

| <u>Criteria</u>            | <u>Calculation</u>   | <u>Vulnerable</u> | <u>Resilient</u> | <u>Agile</u> | <u>Customer<br/>3 Year<br/>Average</u> |
|----------------------------|--|-------------------|------------------|--------------|--|
| Debt/Asset Ratio           | $\frac{\text{Total Farm Liabilities}}{\text{Total Farm Assets}}$   | >70%              | 40-70%           | <40%         |  |
| Term Debt/EBITDA           | $\frac{\text{Total Term Debt (non-operating)}}{\text{EBITDA}^1}$   | >6:1              | 3:1-6:1          | <3:1         |  |
| Working Capital/Expenses   | $\frac{\text{Current Assets} - \text{Current Liabilities}}{\text{Total Farm Expenses}}$  | <10%              | 10-33%           | >33%         |  |
| Operating Expenses/Revenue | $\frac{\text{Operating Expenses}^2}{\text{Total Farm Revenue}}$  | >85%              | 75-85%           | <75%         |  |
| Coverage Ratio             | $(\text{Net Farm Income} + \text{Interest} + \text{Depreciation} + \text{Total Non-Farm Income} - \text{Income Tax Expenses} - \text{Family Living Withdrawals}) / \text{Total Annual Principal \& Interest Payments on Term Debts \& Capital Leases}$ | <110%             | 110-150%         | >150%        |  |

<sup>1</sup> EBITDA = Net Farm Income + Interest + Depreciation

<sup>2</sup> Operating Expenses Excluding Interest and Depreciation

# Bridge or Pier Concept

- Before:  $\frac{\text{Term Debt} = \$1,000,000}{\text{EBITDA} = \$250,000} = 4 \text{ to } 1$
- After:  $\frac{\text{Term Debt} = \$1,250,000}{\text{EBITDA} = \$250,000} = 5 \text{ to } 1$
- no improvement in EBITDA
- refinancing using land equity
- debt levels higher
- owner equity loss, more debt service
- water is deeper near the end of pier
- the longer the pier, then the narrower the pier



# *Final Thoughts*

- everyone counts
- ARE's
- training and development
- A & P's of customer service
- build best relationships in the down times
- consistency of values of Farm Credit System



# *Staying Positive in the Down Cycle*

- network of people = self worth + net worth
- older – mentor and wisdom
- education and development
- take a look at yourself
  - exercise
  - hear the silence
- giving back
- sweat the small stuff
- position for small accomplishments