GETTING A GRIP ON AGRICULTURE AND THE ECONOMY

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Macro Clinic Video Blog: www.compeer.com/education
Road Warrior of Agriculture: www.cornandsoybeandigest.com
Ag Globe Trotter: www.northwestfcs.com
Dave’s GPS & Dashboard Indicators: www.farmermac.com

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Walking the Line—“Fresh Start 2020”

Five Positives in Agriculture

- low, stable interest rates
- stable energy cost
- market volatility, proactive base hits
- land value stability & resilience
- accelerated generational transfer –
  - young farmers, ranchers and green shoots
Walking the Line-“Fresh Start 2020”

Five Challenges in Agriculture

- dependence on government income
- loss of international markets/market competitiveness
- global political posturing/change
- alternative agriculture, consumer demand shifts
- consolidation backlash
Perspectives on the New Decade

- more change in the next decade than the last 70 years
  - technology, consumers & management
- economic & financial volatility
  - friend: proactive manager
  - foe: reactive manager
- business IQ is the common denominator for success
- decade of transitions
  - capital, human assets & business culture shifts
- more opportunity for success or failure depending on your mindset, capitalizing and controlling your destiny
- balance “high tech” with “high touch”
  - high tech- biotech, engineering, big data
  - high touch- in the moment, interpersonal skills, interdependent
### Eras & Cycles: Fork in the Road

<table>
<thead>
<tr>
<th>Decade</th>
<th>Era of Economics</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950’s - 1960’s</td>
<td>Post War, Go-Go Production Era</td>
</tr>
<tr>
<td>1970’s</td>
<td>Go-Go Economics Era</td>
</tr>
<tr>
<td>1980’s</td>
<td>No Go Economics Era</td>
</tr>
<tr>
<td>1990’s</td>
<td>Slow Go Economics Era</td>
</tr>
<tr>
<td>2000’s</td>
<td>Go-Go Super Cycle Era</td>
</tr>
<tr>
<td>Teen Years</td>
<td>Slow &amp; No Go Economics Era</td>
</tr>
<tr>
<td>Adult Years</td>
<td>Fork in the Road Management &amp; Economics Era</td>
</tr>
</tbody>
</table>
Economic Radar Screen - Globalization vs. Decoupling

- international trade
  - USMCA
  - China’s Belt & Road Initiative
- synchronized global economic moderation
  - 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.
By Mid-June, Longest Economic Expansion in the U.S.

Longest economic expansions in modern U.S. history
(As of January 2020)

1991 to 2001: 120 months
2009 to present: 126 months
1961 to 1969: 106 months
1982 to 1990: 92 months
1938 to 1945: 80 months
2001 to 2007: 73 months

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

- signs to watch for
- timing
- causes
- length and depth
- impact on agriculture
- how to prepare
## Top Five Economic Indicators

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Growth</th>
<th>Neutral</th>
<th>Recession</th>
</tr>
</thead>
<tbody>
<tr>
<td>LEI/Diffusion Index</td>
<td>Positive</td>
<td>Flat/Decline</td>
<td>Decline 0.3% for 3 consecutive months AND &gt;1% overall</td>
</tr>
<tr>
<td>Consumer Sentiment</td>
<td>&gt;90</td>
<td>80-90</td>
<td>&lt;80</td>
</tr>
<tr>
<td>Housing Starts</td>
<td>1.5 Million</td>
<td>1.0-1.5 Million</td>
<td>&lt;1.0 Million</td>
</tr>
<tr>
<td>PMI</td>
<td>&gt;50</td>
<td>41.7-50</td>
<td>&lt;41.7</td>
</tr>
<tr>
<td>Stock Market</td>
<td>10% increase</td>
<td>Flat</td>
<td>&gt;30% decrease</td>
</tr>
</tbody>
</table>
Mega Trends 2020-2030

- alternative products - meat & milk continue to grow/mature
- production increases worldwide
  - technology
  - new land/resources in use
  - weather
- loss of export market share
- land value commodity
  - price disconnect
- NGO's bigness under attack
- government supports continue
- energy and oil prices stability
- young farmers/ranchers/women/minorities/veterans
- urban agriculture
- other
Net Farm Income, 2018

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
Business IQ: Spectrum of Performance Possibilities

1. High Working Capital
2. Low Working Capital
3. High Equity & High Efficiency
4. Low Equity & Low Efficiency
5. High Profits & Cash Flow
6. Low Profits & Cash Flow

- Code Green: 35+ B. IQ
- Code Yellow: 20-34 B. IQ
- Code Red: < 20 B. IQ
- Code Orange: 20-40 B. IQ

B. IQ = Business IQ
Paddling - Upper Right Quad.  
**Code Green - Disciplined Growth**

- strong business IQ score of 35+
- proactive manager
- > 60% equity
- term debt to EBITDA <2.5:1
- operating expense/revenue ratio (excluding interest and depreciation) <75%
- working capital to expenses >30%
Treading Water - Upper Left Quad.

**Code Yellow - Limited Growth**

- moderate business IQ score of 20-34
- 70% equity
- working capital to expenses >20%
- operating expenses/revenue ratio (excluding interest and depreciation) >80%
- competitive issues in industry
Paddling or Bailing Water – Lower Rt.
Code Orange - Excessive Growth

Paddling towards **Green**
- business IQ score >38
- ROA averages 6%
- <50% equity
- modest family living expenses
- dimensional revenue streams
- earns and turns

Bailing towards **Red**
- business IQ score of <28
- profit issues- ROA averages 1%
- <50% equity
- high living costs
- specialized revenue streams
- lack earns & turns
Bailing Water - Lower Left Quad.

**Code Red - Partial or Total Liquidation**

- poor business IQ score of <20
- reactive manager
- <40% equity
- working capital is negative
- operating expense to revenue over 90%
- excessive family living expenses
- victims & “know-it-alls”
## 2020 Winter Renewal Season Dashboard

<table>
<thead>
<tr>
<th>Criteria</th>
<th>Calculation</th>
<th>Vulnerable</th>
<th>Resilient</th>
<th>Agile</th>
<th>Customer 3 Year Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating Expenses/Revenue</td>
<td>Operating Expenses¹ Total Farm Revenue</td>
<td>&gt;85%</td>
<td>75-85%</td>
<td>&lt;75%</td>
<td></td>
</tr>
<tr>
<td>Term Debt/EBITDA</td>
<td>Total Term Debt (non-operating) EBITDA²</td>
<td>&gt;6:1</td>
<td>3:1-6:1</td>
<td>&lt;3:1</td>
<td></td>
</tr>
<tr>
<td>Working Capital/Expenses</td>
<td>Current Assets - Current Liabilities Total Farm Expenses</td>
<td>&lt;10%</td>
<td>10-33%</td>
<td>&gt;33%</td>
<td></td>
</tr>
<tr>
<td>Coverage Ratio</td>
<td>(Net Farm Income + Interest + Depreciation + Total Non-Farm Income – Income Tax Expenses-Family Living Withdrawals) / Total Annual Principal &amp; Interest Payments on Term Debts &amp; Capital Leases</td>
<td>&lt;110%</td>
<td>110-150%</td>
<td>&gt;150%</td>
<td></td>
</tr>
</tbody>
</table>

¹ Operating Expenses Excluding Interest and Depreciation
² EBITDA = Net Farm Income + Interest + Depreciation
Financial Trip Points

- split lines of credit
  - > 10 lines
- term debt/EBITDA 6 to 1 or more
  - 3 to 5 years earnings on average
- burn rate on core equity <2.0 years
- operating expense/revenue ratio excluding interest & depreciation above 95% (three year average) with no non-farm income
- victim, know it all attitude concerning business improvement
Producers: Advice Given But Least Listened to or Followed in Practice

- working capital to expenses greater than 25% with 20% of current assets in cash- “dry powder”
- developing, following & monitoring projected cash flow to actual results
- drop dead exercise in transition management
- written goals- “the six degrees”
- hire for attitude, train for aptitude
- indistractables- mental vs. physical health/hygiene
- separate business & personal living budgets
- develop a written business plan that is executed and monitored
- establish regular quarterly meetings with advisory team
- net work of people = financial and mental net worth
Lenders: Advice Given But Least Listened to or Followed in Practice

- most financial issues start outside of the numbers
- global family living cost concept
- credit scoring model is great tool but not the gospel
- trust but verify inventory, payables & other liabilities
- don’t be a perfectionist on accruals, just ask questions
- fear of lender liability – advice vs. alternatives
- emotional drainer- “victim vs. know it all attitudes”
- growth and expansion- 25% rule
- indistractables
- lender cost cutting vs. investment in training
<table>
<thead>
<tr>
<th>Products</th>
<th>Term</th>
<th>Amortization</th>
<th>Choice Reset Margin</th>
<th>Standard Rates</th>
<th>Choice Rates</th>
</tr>
</thead>
<tbody>
<tr>
<td>5-year VRM</td>
<td>15</td>
<td>15</td>
<td>15</td>
<td>3.54%</td>
<td>3.19%</td>
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<tr>
<td>5-year VRM</td>
<td>25</td>
<td>25</td>
<td>25</td>
<td>3.55%</td>
<td>3.20%</td>
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<tr>
<td>7/1 ARM</td>
<td>15</td>
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<td>3.25%</td>
<td>3.58%</td>
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<tr>
<td>10/1 ARM</td>
<td>15</td>
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<td>3.25%</td>
<td>3.81%</td>
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<tr>
<td>10-year VRM</td>
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<td>4.16%</td>
<td>3.81%</td>
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<td>10-year VRM</td>
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<td>4.22%</td>
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<td>15-year VRM</td>
<td>20</td>
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<td>20</td>
<td>4.30%</td>
<td>3.95%</td>
</tr>
<tr>
<td>15-year VRM</td>
<td>25</td>
<td>25</td>
<td>25</td>
<td>4.39%</td>
<td>4.04%</td>
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<tr>
<td>7-year Fixed</td>
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<td>15</td>
<td>3.72%</td>
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<td>15-year Fixed</td>
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<td>4.05%</td>
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<td>15-year Fixed</td>
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<td>4.34%</td>
<td>3.99%</td>
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<td>20-year Fixed</td>
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<td>4.24%</td>
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<td>25-year Fixed</td>
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<td>25</td>
<td>4.39%</td>
<td>4.04%</td>
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<tr>
<td>30-year Fixed</td>
<td>30</td>
<td>30</td>
<td>30</td>
<td>4.51%</td>
<td>4.16%</td>
</tr>
</tbody>
</table>

As of 1/16/2020
Thank you!

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