

# ECONOMIC SHOCKWAVES: CHALLENGES & OPPORTUNITIES



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# 1978 to 1979 Déjà vu

- High oil prices
- International ag market uncertainty
- Spiking land values
- Stagflation
- Political & military uncertainty
- Technology acceleration



# The State of the U.S. & Global Economies (1)

- Ukraine Russia military conflict
  - 29% of world's wheat
  - 14% of global corn exports
  - 80% sunflower exports
  - Russian oil to India & China
  - Fertilizer: potassium & nitrogen
  - One to five years disruption for energy & food
  - One to five years for technology & infrastructure for natural gas exports to Europe



# The State of the U.S. & Global Economies (2)

- Food nationalism
  - Export restrictions
- 50 countries dependent on Russia & Ukraine for more than 30% of imported wheat
- Egypt & Turkey > 60% imports from Russia & Ukraine
- Geo political risk
  - Authoritarian & emerging economics vs. the west & rich nations
    - Wear down the west strategy
    - Create economic havoc in the rich nations
    - Create regional social unrest



# The State of the U.S. & Global Economies (3)

- Energy security & green energy transition
  - Fossil fuel imbalances
  - Flip the switch on government policies
  - Regions of the world - climate is secondary to the economy
  - Watch the U.S. midterm elections this fall



# Federal Reserve & World Central Banks' Panic

- Wealth creates cycle 1970-2021
- Wealth destruction cycle 2022- ???
- Mama Bear & Papa Bear levels- “outlook”
  - Stock market
  - Cryptocurrency
  - Housing & real estate
  - Farm real estate
- Behavioral economics in full swing





# Federal Reserve Dilemma – Core & Headline Inflation- “Hard Habit to Break”

- Supply chains
- Weather
- Government stimulus savings
- Oil & energy
- Geographic wealth shifts
- Deglobalization
- Federal reserve- “the villains”



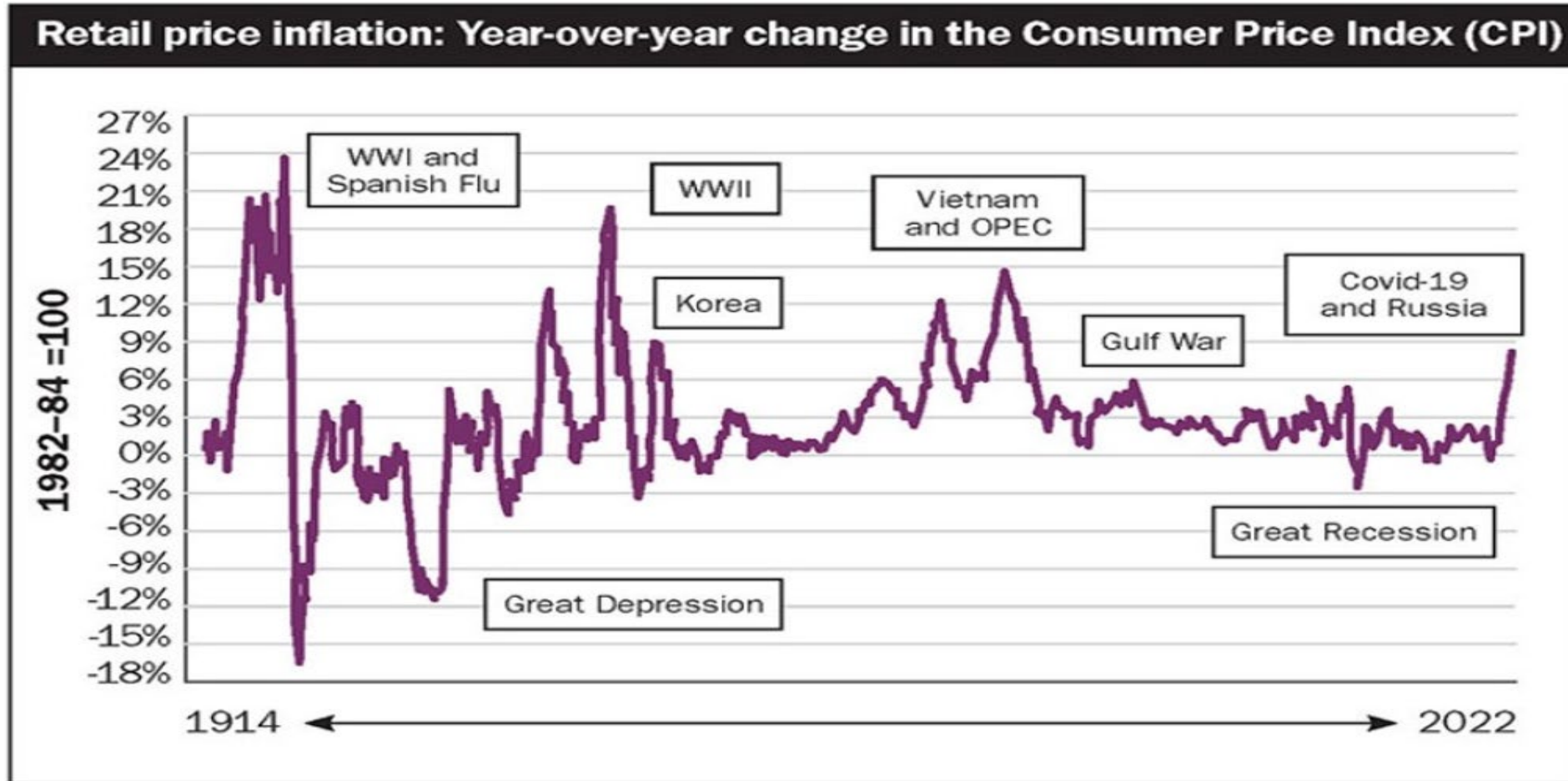
# Interest Rates – How High? When is the Next Recession?

- Average rate increase 2.53%
- Maximum rate increase 4.75%
- Unemployment rates- a lag indicator
- Early 2023 possible global recession
- Stagflation





# Retail Price Inflation



**Source:** "Which prices go up and why?" by Andrew M. Novakovic [Which prices go up and why? \(hoards.com\)](https://hoards.com/which-prices-go-up-and-why/)

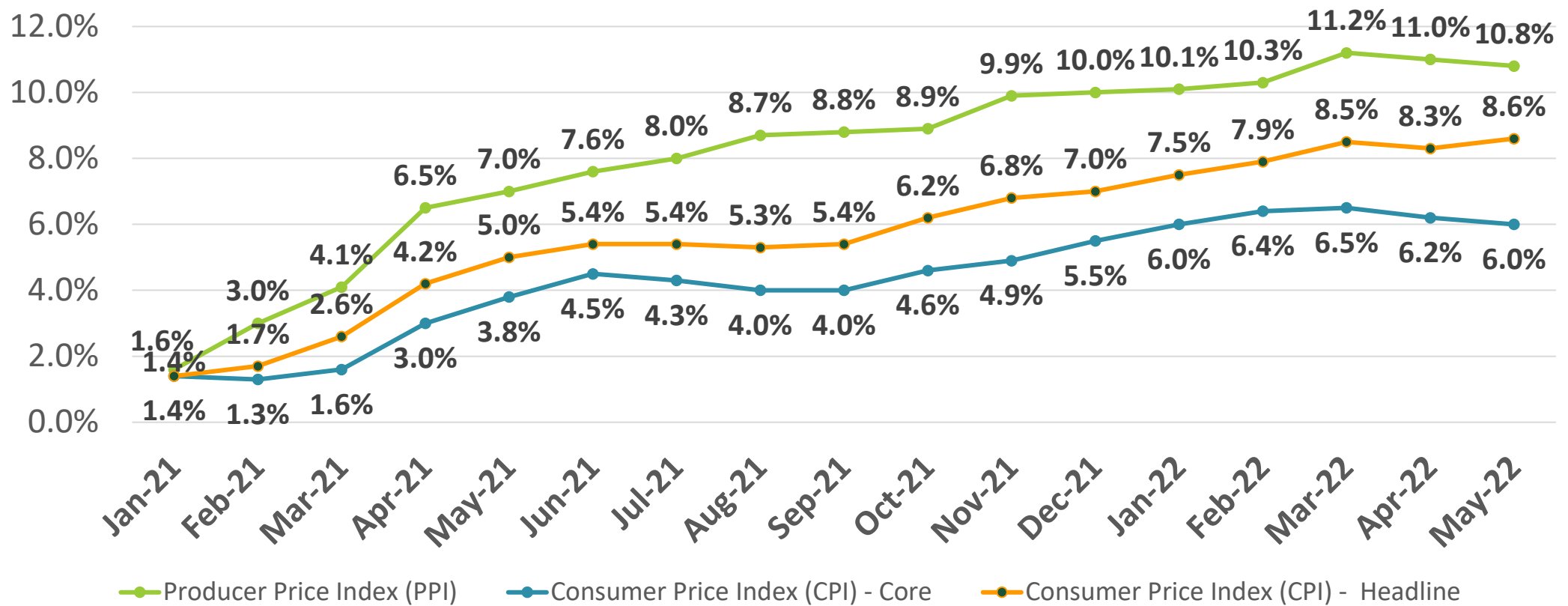
# Recent Inflation Rates

<u>Month</u>	<u>PPI</u>	<u>CPI Core</u>	<u>CPI Headline</u>
January 2021	1.6%	1.4%	1.4%
February 2021	3.0%	1.3%	1.7%
March 2021	4.1%	1.6%	2.6%
April 2021	6.5%	3.0%	4.2%
May 2021	7.0%	3.8%	5.0%
June 2021	7.6%	4.5%	5.4%
July 2021	8.0%	4.3%	5.4%
August 2021	8.7%	4.0%	5.3%
September 2021	8.8%	4.0%	5.4%
October 2021	8.9%	4.6%	6.2%
November 2021	9.9%	4.9%	6.8%
December 2021	10.0%	5.5%	7.0%
January 2022	10.1%	6.0%	7.5%
February 2022	10.3%	6.4%	7.9%
March 2022	11.2%	6.5%	8.5%
April 2022	11.0%	6.2%	8.3%
May 2022	10.8%	6.0%	8.6%

\*% change in last 12 months

# Recent Inflation Rates

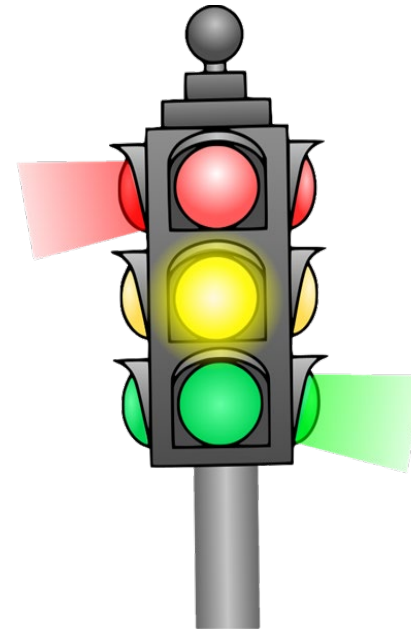
## (% Change in Last 12 Months)



Source: U.S. Bureau of Labor Statistics

# Lender & Business Dashboard Watch List

<u>Indicator</u>	<u>Range</u>	<u>Light</u>
Copper Prices	\$3.75 to \$5.00/Pound	Red
Consumer Sentiment	50.2 to 72.8	Red
LEI / Diffusion Index	Downward trend	Yellow
Purchasing Managers Index	Low 50's	Yellow
Housing Starts	>1.5 Million	Green
Unemployment	3.6% U-3/7.1% U-6	Green
Factory Utilization	75% - 78%	Green
Federal Debt	Approximately \$30 Trillion	Red
Oil Prices	\$65 to \$125/Barrel	Yellow
Yield Curve	Flat to Inverted	Red



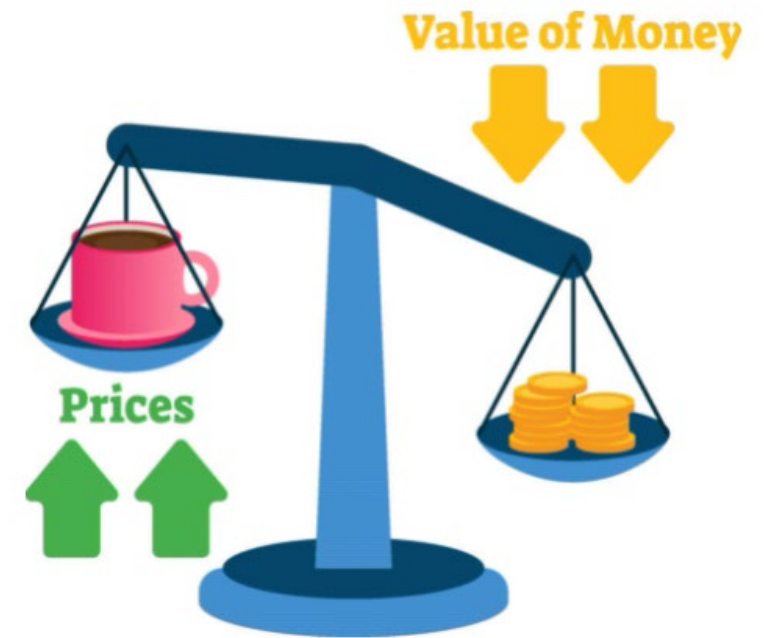
# Variables That Could Lead to or Cause a Farm Recession

- Bear market in land values
  - Mama bear- 20% regional or national decline
  - Papa bear- 40-50% regional or national decline
- Farm & ranch financial liquidity crunch
  - Economic flip- prices decline faster than cost, margin compression, negative margins, interest rate increases reduces margins
- Institutional panic
  - Federal & state regulatory directives
  - Tightening of underwriting lending standards



# Top Performing Producers Response to Inflationary Volatile Times

- Prudent cost management & expense management
- Maintain strong levels of liquidity
- Retaining cash reserves
- Diligence in developing & monitoring cash flows
- Informed & objective grain & livestock marketing decisions
- Just in time to just enough
  - Alternative avenues
  - Proactive planning
  - Multiple suppliers



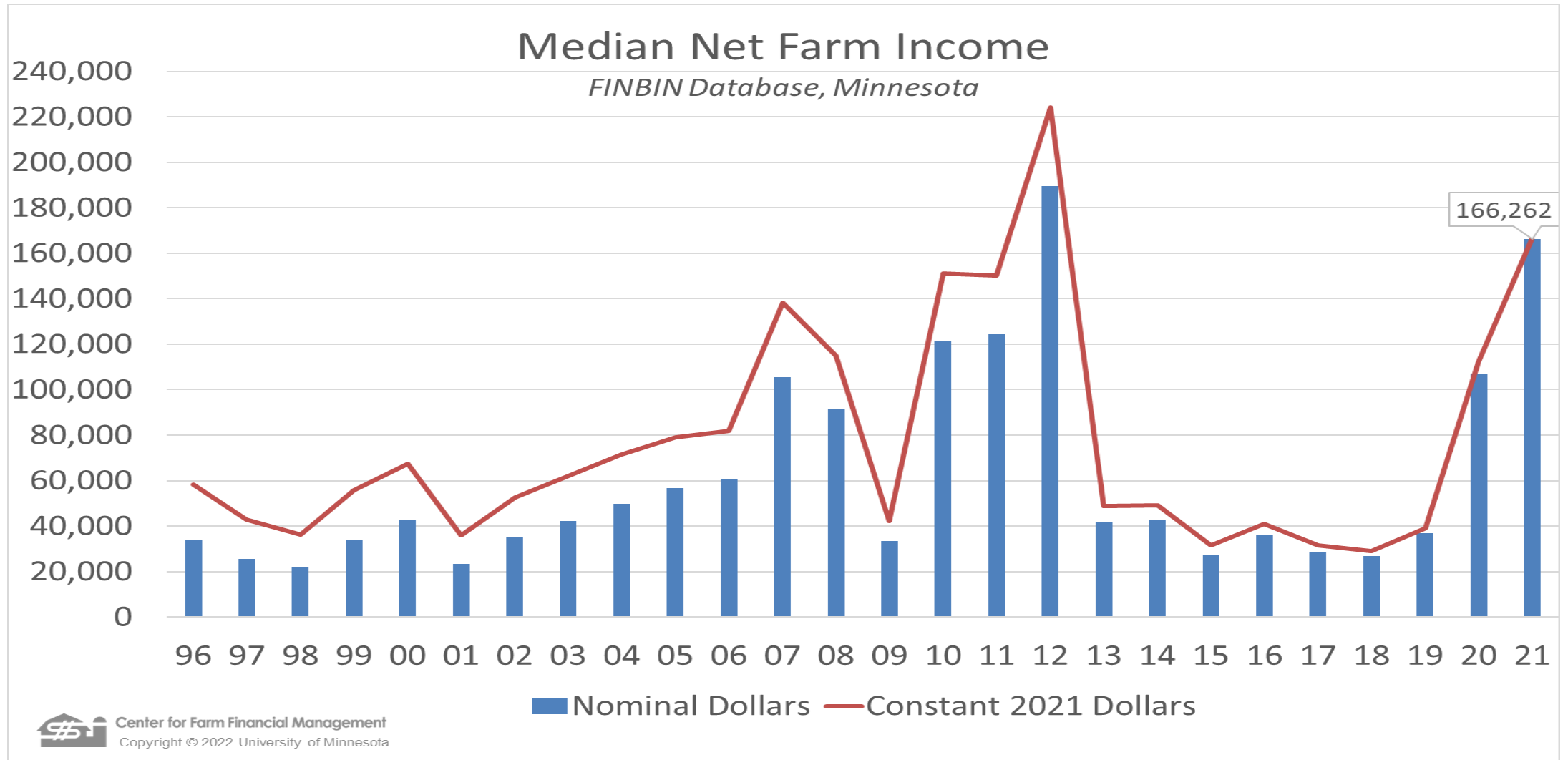


# Bottom Performing Producers Response to Inflationary Vulnerable Times

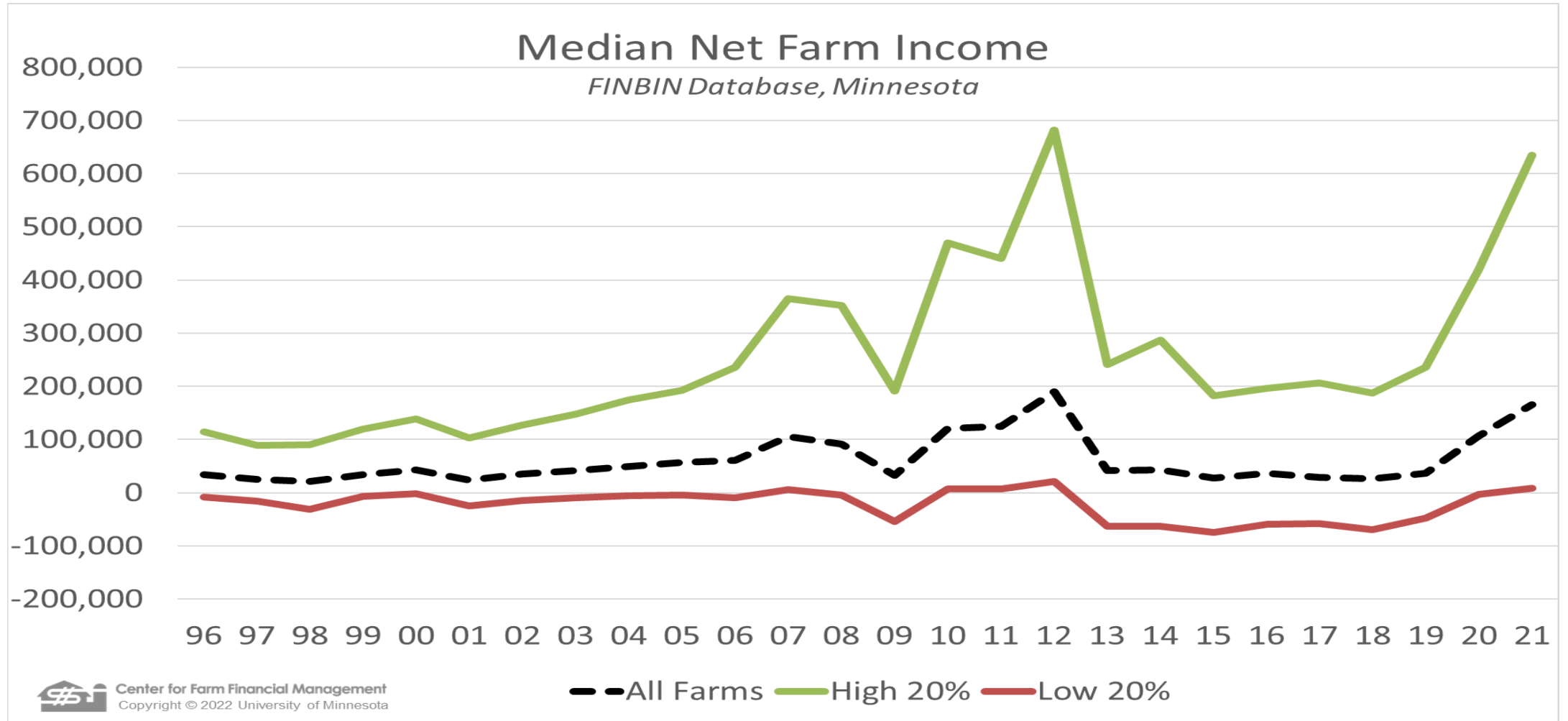
- Least cost method of producer
- Distributions for capital investments for tax reasons
- Draining equity/refine operating debt
- Paying higher land rents on previous young managers
- Reactive & emotional decision making
- Borrow more operating money for 2022
  - Living cost
  - Capital Expenditure Needs
  - Higher land rents
- Do what I've always done. "The government will take care of me."



# Median Net Farm Income



# Median Net Farm Income



# How Do Farms Stack Up Historically? 2012-2021

## Historical information for Southwest, South Central & Southeast Minnesota

The source of the green, yellow, and red credit risk rating is from "Weighing the Variables" by David M. Kohl. He considers the six (6) color coded factors below to be key indicators of financial credit quality.

Green	The farm business enjoys a competitive position
Early Yellow	The farm business has some early caution signs
Late Yellow	The farm business has some major caution signs
Red	The farm business could face some major obstacles

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Current Ratio - Multiple-Enterprises</b>										
Top 10 Percent	3.21	2.37	2.12	2.28	2.30	2.24	2.22	2.30	2.69	2.92
High 20 Percent	2.90	2.40	2.24	2.21	2.21	2.11	2.20	2.20	2.39	2.83
Average Farms	2.50	2.03	1.79	1.64	1.62	1.57	1.51	1.51	1.98	2.47
Low 20 Percent	1.48	1.60	1.23	1.23	1.19	1.12	1.07	1.07	1.23	1.75
<b>Farm Debt to Asset Ratio (Market)</b>										
Top 10 Percent	38%	39%	42%	38%	39%	40%	39%	40%	40%	41%
High 20 Percent	40%	38%	40%	39%	40%	41%	39%	41%	41%	41%
Average Farms	42%	40%	43%	45%	45%	45%	46%	46%	44%	44%
Low 20 Percent	51%	46%	52%	54%	54%	53%	55%	54%	51%	51%
<b>Rate of Return on Farm Assets - Rent/Lease Majority of Assets (Cost)</b>										
Top 10 Percent	17.9%	7.8%	12.5%	5.8%	5.8%	6.8%	5.9%	7.8%	12.3%	15.7%
High 20 Percent	17.3%	7.4%	10.4%	5.2%	5.6%	6.3%	5.2%	7.2%	11.4%	15.1%
Average Farms	13.7%	2.6%	3.7%	0.8%	1.4%	1.9%	1.0%	3.4%	7.8%	11.4%
Low 20 Percent	1.0%	-6.2%	-5.5%	-5.2%	-4.0%	-3.8%	-4.0%	-3.4%	-1.7%	-0.4%
<b>Term Debt Coverage Ratio</b>										
Top 10 Percent	540%	236%	336%	197%	199%	215%	233%	273%	403%	574%
High 20 Percent	491%	218%	297%	178%	190%	203%	208%	246%	375%	553%
Average Farms	363%	102%	133%	77%	90%	102%	91%	148%	274%	389%
Low 20 Percent	94%	67%	47%	-46%	-20%	-13%	-21%	3%	72%	109%
<b>Operating Expense Ratio</b>										
Top 10 Percent	57.6%	73.2%	73.3%	73.8%	72.7%	72.8%	72.7%	73.3%	67.4%	62.6%
High 20 Percent	59.9%	72.5%	73.8%	74.5%	73.8%	74.2%	74.7%	74.3%	68.4%	62.5%
Average Farms	64.7%	81.4%	79.8%	84.6%	83.0%	82.3%	84.3%	79.4%	71.2%	66.6%
Low 20 Percent	86.3%	99.9%	99.2%	99.6%	96.2%	96.6%	97.4%	95.3%	89.2%	87.9%
<b>Interest Expense Ratio</b>										
Top 10 Percent	2.5%	2.9%	2.2%	3.0%	3.3%	3.2%	3.9%	3.4%	2.8%	2.0%
High 20 Percent	2.7%	3.1%	2.4%	3.2%	3.5%	3.4%	3.9%	3.7%	3.1%	2.2%
Average Farms	3.4%	3.9%	3.7%	4.2%	4.6%	4.8%	5.4%	5.2%	4.3%	3.1%
Low 20 Percent	5.4%	4.5%	6.1%	4.7%	5.4%	6.1%	6.6%	7.8%	8.2%	5.1%



MINNESOTA STATE



South Central College



RIVERLAND  
Community College

# Financial Liquidity & Cash as a Bridge

- Cash is trash - ☹️ Wall Street Journal perspective
- Financial liquidity is choke point
  - Nation- “Russian example”
  - Business- “financial & farm crisis”
  - Personal household- “Dave Ramsey rule”
- Financial liquidity- buffer to preserve wealth- sale of discounted assets
- Financial liquidity- opportunity positioning- purchase discounted assets



# Debt Strategies for Economic Cycles

- Term Debt/EBITDA (Earnings before interest, taxes, depreciation & amortization)
  - < 3:1 Green light
  - 3:1 to 6:1 Yellow light
  - >6:1 Red light
- Debt to asset exceeds 50% five conditions:
  - Top 25% in production & cost efficiency
  - Modest personal withdrawals
  - Working capital backup
  - Marketing risk management plan
  - Luck with weather, disease, etc.
- Sound relationship agricultural lender
  - Conservative at top of the economic cycle
  - Courageous at bottom of the economic cycle
  - Consistent all the time
  - Understands industry, business and personal goals





# Operational Efficiency Strategy

- EBITDA/Revenue
  - >30% Green light
  - 10 to 20% Yellow light
  - <10% Red light



# Business Development Opportunities

## 2022 Survey of Agricultural Lenders

- Increased lines of operating credit
- Family businesses in transition
  - Alignment with younger generations
- Smaller, part time & lifestyle farm businesses
- Land purchases & acquisitions
- Financial statement analysis & benchmarking to increase return on relationship
- Retention of productive lending staff



# Wisdom for Bankers

- Be a student of credit the (science or numbers) but balance it with the art of lending (human behavior).
- Credit issues often start in the top of the economic cycle. Business development often happens in the economic down cycle.
- Economic & financial greed has a cousin called fraud.
- Hire for attitude, train for aptitude but hold people accountable.
- A lender with championship DNA makes training & education a high priority.



# Q&A with Dr. Kohl

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## Online Articles:

- Road Warrior of Agriculture

<https://www.farmprogress.com/road-warrior>

- Ag Globe Trotter

<https://www.northwestfcs.com/ag-industries/economic-updates>

- Dave's GPS & Dashboard Indicators

<https://www.farmermac.com/news-events/daves-gps/>

