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What are my Options to Grow?

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There are numerous motivations for farms to expand their businesses. Even in today's environment of tight margins, many farms are exploring expansion options. When exploring these options, it is important to address key questions pertaining to the farm's strategy. A previous *farmdoc daily* article discussed ten questions that should be addressed when examining challenges and opportunities associated with farm growth. This article focuses on the second question: what are my options to grow.

Strategic Options for Farm Growth

As strategic options are assessed there are numerous growth and downsizing alternatives that are available (Miller, Boehlje, and Dobbins, 1998). The discussion below will focus on the following nine alternatives: focus/specialize, intensify/modernize, expand, diversify, replicate, integrate, network, delay/wait and see, and downsize. The first six options focus on farm growth while the last three explore non-growth options.

The first option is to focus or specialize. Many farms like to stick to what they know. This option allows the farm to focus managerial time on improving efficiency and reducing cost. Lower cost producers tend to have the ability to stay competitive. Concentrating on one activity (e.g., producing crops), can aid in cost reduction through a more intensely managed operation.

The second option is to intensify or modernize. This option typically involves producing more output with the same fixed asset base. A more intensely run operation spreads fixed costs over greater output, lowering overall cost of production per unit produced and improving the asset turnover ratio. This option often involves the adoption of modern production technologies.

The third option is to expand. The most common strategic move for many farms is expansion of facility size or acres. Though commonly used, this option should only be pursued after all possible efficiencies have been exploited. Expanding an inefficient operation can lead to a larger inefficient operation.

The fourth option is to diversify. Diversification involves the addition of new enterprises. In addition to potentially reducing overhead costs per unit produced, this option can also reduce risk. Due to the fact that economic forces that affect one agricultural enterprise affect others, this option may not be as advantageous for risk reduction as one might think. Diversification can also cause management time to be spread too thin across enterprises. If even risk reduction is small, diversification may improve the utilization of underutilized skills and resources and reduce overhead costs per unit produced. If a farm is serious about reducing risk, then the alternatives considered should include investments that are not subject to the same fundamental economic forces that impact agriculture. Such alternatives might include stocks or mutual funds, bonds, non-agricultural businesses, or residential or commercial real estate. Expertise should be obtained in choosing among these investments, just like the best information and expertise is used to choose among various farm or agricultural investments.

The fifth option is to replicate the existing operation on a different site rather than expansion of the current unit. This option allows for decentralized management in smaller units. It also reflects the fact that it may be difficult to find the acreage to expand in the location of the current unit.

The sixth option is to integrate by moving forward, backward, or horizontally into production or processing. Examples would include finishing hogs, producing turkeys, or producing eggs under contract. These examples have implications on farm net returns and risk.

The seventh option is to network. Expanding a single farm to the size where size benefits are available is not always the most prudent option. Networking allows a group of smaller operations to look like a larger operation in the marketplace. Examples of networks include buying groups, machinery sharing arrangements, and utilizing personnel, including operators, across farms.

The eighth option is to delay farm growth. A farm's management team may survey current conditions and determine that they are not sure what direction to take. In the short-run, inaction may have merit. "Buying time" may provide for new opportunities to manifest themselves. If this strategy is pursued, it is still important to develop a decision trigger that will result in action.

The ninth strategy is to downsize. There are many in farming who are surveying their situation and wondering if continuing to operate at the current size or a larger size is the most logical plan. Therefore, one strategic size option is to reduce the size of the business. The decision to downsize the business is often linked with a strategy to exit from the business, but this need not be the case. Downsizing may help improve the focus of the business or the efficiency of the business.

Choosing a Farm Growth Option

A sequential framework can be used to think about the nine growth options. The first decision is to either move toward making a decision or delay. If a farm chooses the delay option, it should establish a decision trigger that will cause the farm to move toward a decision. The second decision is to choose between strategies that will improve the business or exiting. If the decision is to improve, an initial step is to review the focus of the business. This will lead the farm to strategies to intensify, expand, or downside the business. Remember that expansion should only be considered when all existing efficiencies have been exploited. Once a farm has garnered the maximum advantages from the existing operation, it should consider additional ways to improve or expand the business. These may include diversification, replication, integration, or networking.

The discussion pertaining to risk above focused on the variability of net returns and downside risk. Growth options also involve strategic risk. As indicated by Boehlje and Langemeier (*farmdoc daily*, May 5, 2017), strategic risk involves the sensitivity of the farm's strategic direction and ultimate vulnerability and sustainability of the farm to uncertainties in the business climate. One of the ways to assess strategic risk is to use scenario analysis. Farms exploring alternative growth and downsizing options are encouraged to use scenario analysis to gauge the impact of each alternative on the farm's balance sheet and income statement.

Conclusions

Farms have numerous options that can be explored when examining farm growth and downsizing decisions. When evaluating alternatives it is important to gauge the impact of each alternative on net returns, risk, and the farm's resource base. Future articles will explore strategic issues and financial considerations pertaining to farm growth.

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