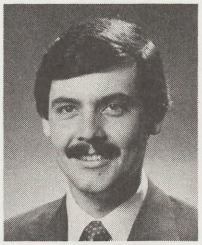

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What borrowers look for in an agricultural lender

by Michael A. Jackson

"I see credit as a real competitive area. There are many sources around. Some of them can work with you . . . some of them don't want to work with you. Some of them say, 'If you want money, come to us.' Others will come out and work with us. So this ability to work with the person who's borrowing money is extremely important."

Mark S., a Minnesota farmer

Agriculture has always meant change—who was farming, who owned the land, how it was managed, which crops were grown, and how much the government interfered with or supported innovative production practices and healthy commodity markets. Today is no exception.

Three distinct groups

Many researchers and futurists now speak of at least three distinct groups of farmers, each with its own buying patterns, production practices and values:

1. traditional "family farms" for whom continued production with well-proven methods on a limited acreage base provides marginal (and often government-dependent) income;

2. part-time or sundown farmers for whom off-farm income is a primary source of support;

3. "superfarmers" or producers who run the farm—whether as a family corporation or a farm manager—strictly as a profitable business, by seeking maximum economies of scale, often within speciality crop or livestock operations. An active attempt at some vertical integration (feed - farrow - finish - market) or diversification of enterprises (seed or fertilizer dealer) helps insulate the operation from downturns common in the ag economy.

These three groups of borrowers are fundamentally different. They make the decisions that guide their operations on the basis of different values and different potential financial goals. They do not use the information available about production science and marketing equally well. They adopt technology at different paces. When they make borrowing decisions, like all their input decisions, they look for someone to "work with them," in the words of the young Minnesota farmer quoted in the beginning of this article. However, "working with them" may mean very different things to each group, because each group works out its decisions in different ways.

The traditional family farm

Of these three groups, the traditional family farm is a well-known lending customer. Their problems over the last 5 to 10 years have been well-documented by both agricultural lending professionals and the popular press. At the risk of oversimplifying what were often difficult decisions, they and their lenders based borrowing decisions on the value of their assets. As a result, they may have over-borrowed as inflation artificially inflated asset value. Some farmers in this category were lulled by that temporary increase in net worth and the subsequent farm-support programs, into complacency about new technologies and the value of increased productivity.

This traditional borrower may harbor some resentment against the credit industry, blaming lenders for his own willingness to measure productivity in paper profits and growth as paper assets. And yet, this group still is among the most loyal agricultural borrowers. They tend to value community relationships and traditions. They expect to be valued as long-standing customers, and like to be well known. While some may dislike submitting cash flows and financial statements, most have now accepted these procedures as part of doing business with traditional lenders and even with local suppliers offering credit.

"This traditional borrower may harbor some resentment against the credit industry."

In short, these borrowers still look for many of the same qualities they always have wanted: a local lender specializing in agriculture and familiar with their operation and their needs; a lender who is as "loyal" to them as they have been over past years; a lender who understands the predicament farmers like them face today, and will counsel them about ways to keep their family farm.

The sundown farmer

The part-time or sundown farmer is a relatively new "customer" for many lenders. In some cases, these are farms that have become simply too small or too unprofitable to sustain themselves. Outside income provides badly needed stability to cash flow the operation and to retire debts that threaten the existence of the farm. In these cases, the farmers' need for better financial planning often was one cause of their problems. A severe financial situation may make a farmer realize how his bank can help him, "work with him," to shore up a shaky financial condition. In such cases, the "loyalty" of the lender is a paramount consideration, and an honest relationship is important to both farmer and lender.

In other cases, the sundown farmer is more of a hobby farmer, coming to farming as a secondary business rather than leaving farming for extra income. These customers often are successful professionals in another field, with skills in business planning, budgeting and marketing. Thus, these customers are likely to look for services in a lender that they cannot provide themselves or that they don't want to provide. Some may want a computerized record-keeping service, and some may need financing for larger capital improvements or technological advances. Production management expertise in financial terms is important to this farmer. In short, these borrowers are already successful businesspeople, and expect a lender to provide a range of services from which they can pick and choose those that fit their management needs.

"An honest relationship is important to both farmer and lender."

Farmers of the future

The third group of borrowers has been called "superfarmers" and "farmers of the future." These producers are defined generally as those with gross receipts over $500,000. As borrowers, they must command the attention of any lender who intends to continue to serve agriculture in the year 2000.

As economic pressure has caused consolidation at both the farm level and the supplier level, this group of growers has increased in numbers, in the percentage of inputs they consume, and in the percentage of outputs they produce. They already are a major group in certain markets, such as fruit and vegetable production, specialty crops and feedlot operations. In other areas, their numbers are smaller, but they are still a powerful influence. These borrowers look to an agricultural lender for:

1. **Capital to improve production capacity.**

Expansion until optimum economic scale is reached, or investment in capital improvements and equipment that will result in improved profitability are both key strategies for this group. Rather than basing profitable growth on increased asset values, strategies are aimed at profitable operations. Government programs are understood and used, but economic production is the real goal. Capital must be available at competitive interest rates, to be secured by production efficiency as well as assets.

2. **Information with a focus on profitability.**

The use of consultants of all types is increasing among the "superfarmer" group—from the Delta grower's traditional, crop-protection consultant, to management and financial consultants in the upper Midwest. The use of expert information, whether through a person or through on-line computerized information services and crop-modeling programs, reflects the focus on profitability. Generally, these growers will buy services they cannot reproduce cost-effectively themselves, and will value information from a supplier if they cannot access it cost-effectively from the farm. Thus a wide range of marketing, financial planning and credit services is likely to appeal to these growers, just as they would appeal to any other corporation of their size. The value of an "ag" background is still important because it adds credibility to the consulting services a bank can offer.

"The value of an ag background is still important because it adds credibility."

3. **Value-added services.**

Without value-added services, which meet the needs of this group, their loyalty will waver somewhat. Many of these growers are well-educated or carefully self-taught professional, agribusinesspeople, with diversified enterprise and marketing strategies. They expect the same level of sophistication from their lenders and competitive interest rates. A relationship based upon personal rapport will be insufficient to add value to these customers.

As the 1986 *Transition in Agriculture* study reported, these expectations may open the door for large, non-agricultural banks who can and will provide the capital and associated business services these large operations need.

4. **An overall strategy of risk management.**

The lessons of the last few years will continue to weigh as heavily on these farmers as the lessons of the 1950s and 1930s weighed on their fathers. But these lessons have not taught them fiscal conservatism as much as they have taught farmers the power of responsible borrowing and risk management.

What do borrowers look for in an agricultural lender? They look for someone who can work with them to help them achieve the goals they have set for their operation. However, these goals will be fundamentally different for the sundown farmer, the traditional mid-size to small farmer, and the new breed of superfarmer. Thus, the first step to working with each borrower is to carefully assess his management approach, his goals and his expectations. Only then can a bank respond with an effective marketing approach and identify and develop the services needed for an increasingly diverse customer base.

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