

David M. Kohl

Professor, Virginia Tech

Agricultural Finance and Small Business Management

This is one of a series of articles written by Dr. David Kohl for the Minnesota State Farm Business Management Education Program.

Vol. #106



Quick Hitters and Perspectives

By: Dr. David M. Kohl

We are not conducting a football practice drill or running line sprints in basketball. To conclude this year's series of newsletters, my thoughts will be focused on some of the questions and nuggets that came from my interaction with people on the road, during events, and on webcasts. Let's draw on some of my favorite quick hitters and perspectives.

Who is purchasing farmland in this red-hot nationwide market?

I have a nonscientific 40-40-20 rule regarding farmland acquisition. Forty percent of farm and ranch land is being purchased by growing producers and baby boomer farmers born between 1946 and 1964. Land is the asset of choice as there tends to be a lack of trust in alternative investments such as cryptocurrency, stocks, bonds, and residential real estate. The second forty percent is a combination of farmers and ranchers as well as investors that often are linked to the area or the region. Twenty percent of farmland is being purchased strictly as an investment. The "new kids on the block" are athletes who have moved away from investing in cryptocurrency and real estate on the coasts and are seeking to diversify their portfolios. Expect land appreciation to level off and possibly decline in some areas depending on interest rates, margin compression, and alternative safe investments such as money market accounts, treasury bonds, inflation bonds, and certificates of deposits.

Where are the best opportunities in agriculture?

As we move closer to the quarter-century mark, opportunities in agriculture will not about size, enterprise, or the next big thing. It will be about being a "five percenter," which means being five percent better in many components of production, marketing, risk management, finance, human resources, and operational efficiency. This will be within the scope of your business, family, and personal values and goals. The next generation of agriculture will be made up of more women owners and managers and agri-entrepreneurs that have outside "gig" income that utilize their talents and resources with the management mindset.



Why keep cash in an inflationary environment?

This question was asked by a banker on a snowy day in the Twin Cities this past winter. Many people question maintaining the cash component of working capital with higher levels of inflation. Remember, cash is a tool to be available for resilience, agility, and nimbleness in business strategy.

A producer in the Western U.S. thanked me for saving him \$1 million. He stated that he often disagreed with my suggestion of maintaining strong working capital and cash, but did so reluctantly. When oil prices were negative and diesel fuel was at an all-time low, he used his cash on hand to purchase five years' worth of fuel for his large farm operation and also rented additional storage. Others have indicated that working capital and strong cash levels provide flexibility in marketing plans, enable them to purchase inputs using cash discounts, and allow them to take advantage of deals that require quick timing. Some have stated being able to draw on cash reserves and personal asset values limits the need to sell assets at discounted values when supply exceeds demand. When making plans for this spring and summer concerning cash, remember that working capital and the ability to generate cash is like a queen on the chessboard of business moves. The queen can be there to block adversity, take advantage of opportunities, and be a bridge. You are probably familiar with the old saying about not burning bridges because you may be required to cross them again. This saying is very apropos as far as working capital.

Where are interest rates headed?

The overall goals of the Federal Reserve are price stability and full employment within a growing economy. The central bank will be closely monitoring inflation, with the goal of driving core inflation, excluding food and energy, to two percent and headline inflation, which includes food and energy, to four percent. At the time of this article, the current inflation rates are in the five to six percent range. Should you see inflation moving quickly down toward the Federal Reserve's goals, then the Federal Reserve will pause on interest rate increases. Interest rate declines will come if inflation moves to these levels and the U-3 and U-6 unemployment rates start to increase to 4.5 to 5 percent and 7.5 to 8 percent, respectively. The U-6 unemployment rate includes discouraged workers and people who are underemployed. Another factor to observe is potential negative growth in the United States' gross domestic product (GDP) for at least two quarters. The bottom line is that financial sensitivity testing of interest rates, which have doubled from one year ago, need to be factored in when focusing on the cost of production and cash flow levels.

What are the characteristics of successful young and beginning producers?



I chuckle at the government's attempt to characterize the demographics of beginning farmers and ranchers. My response is that there is no such definition! Some are entering family businesses while others are starting new businesses. Some beginning producers are “boomerangers” starting later in life after other endeavors. With that being said, there are some defining elements that cut across all sectors of successful young and beginning producers.

First, they often keep their overhead costs, both capital and human, low and very efficient. Many new producers leverage off farm income such as “gig” income, W-2 wages, or built-up wealth to be utilized in the agriculture business model. A critical element is low to modest family living costs. Some adjustments in family living costs will be required as a sacrifice for launching and growing the business. Some young and beginning producers returning to family businesses will often start out small with one enterprise to learn the production, marketing, finance, and operation skill sets while utilizing family assets such as machinery, equipment, and, in some cases, land. This is like an internship or apprenticeship to build the management mindset.

Separation of business and personal finances is critical. A personal budget is just as important as a farm budget with a good set of spreadsheets to plan and monitor throughout the year.

An advisory team or mentors can be crucial elements to provide guidance and sanity in a fast-paced world. Just as off-farm revenue provides both income and networking opportunities, a team of advisors and peers can provide exchange and dialogue for critical thinking.

People skills are becoming a much larger component of success. Whether managing labor, suppliers, or commodity and value-added markets, the interdependent versus the independent mindset will be a focus. Personality profiles to understand yourself and others can be invaluable in the communications and the people skills process.

So, you want to go for it on your own? Then \$40,000 to \$70,000 of net income will be necessary. Some producers will generate this level of income on one thousand acres or five acres, while others will need 50 head or 500 head to generate sufficient income. Young and beginning producers are proving that one size does not fit all!

Finally, being intentional with continuing your education is a vital element in the knowledge and information age. Strive each year to attend at least five single or multiple day programs, participate in 10 web or podcasts, and read five magazines, books, or audio books to boost your intellectual collateral, as discussed in previous articles. On YouTube, follow Eric Snodgrass of Nutrien, Ryan Hall, or Roy Ponder. These folks are very good at explaining weather. In particular, Ryan and Roy will give you the weather forecast right down to your area. Peter Zeihan will challenge you on geopolitics in his books *The End of the World is Just*



the Beginning and *The Accidental Superpower*. *The Way of the Shepherd*, *The Ultimate Gift*, and *The Psychology of Money* will make you think about business, finance, and life in general. These books are a must for any future leaders.

As the days get longer and spring brings life to the planet, cherish the sunrises, sunsets, and how those involved in agriculture bring significance in our own way. See you on the road!



MINNESOTA STATE