

Rural Entrepreneurship & Business Development Update



Financial Management

Conventional agricultural lenders are reluctant to make loans to new farmers because they don't know how to estimate the expected cash inflows and outflows from a sustainable farming operation. They understand the financial odds for conventional commodities sold by conventional means at conventional times using conventional farm



inputs and machinery. But, they don't know how much confidence to place in the new farmer's projected production levels because they don't understand organic farming, grass-based livestock operations, or other more natural or sustainable production methods. They don't know how much confidence to place in the new farmer's markets, such roadside stands, farmers markets, CSAs, or direct sales to local food retailers.

New farmers should take every opportunity to educate lenders on the nature of their farming operation and to try to help lenders see that sustainable farming is actually less risky than conventional farming. However, most new farmers are simply going to have to find sources other than conventional commercial lenders to meet most of their financial needs. Perhaps more important, new farmers need to learn to grow their farms at a natural rate and to a natural size. They may need some outside financing to get started and grow to maturity, but shouldn't fall in the trap of borrowing too much money, growing too fast, or growing too large. When new farms reach maturity, they need to focus some of their resources on nurturing other new farms into life and to maturity. A healthy community of new farms will have the capacity to grow from within and will have little need for outside commercial lenders.

CSAs are classical examples of new farmers finding a better alternative for financing their cash flow needs. They ask their customers, rather than lenders, to help match their cash inflow with the farm's cash outflow. They request payments to cover production costs up front, at planting time rather than harvest time. CSA customers also share in the farm's financial risks during the growing season by accepting a share of whatever is produced, rather than contracting for a specific quantity of produce. CSA customers share the risks of crop shortfalls in bad years but share in the bounty of exceptionally good growing seasons.

Acquiring the investment capital needed to start new farms, without access to conventional financing, is a good bit more difficult than meeting cash flow needs. Most new farmers get started in farming by working off-farm for a number of years and saving enough money to buy a small farm, or at least a

sufficiently large down payment to reduce financial risk and make a conventional loan feasible. A significant number of these new farmers are couples who have completed professional careers. Most of these couples have saved some money for retirement and have substantial equity in their house in an urban area with real estate prices. They retire from their careers, sell their house, and buy a house on a small acreage in the country. For younger families that have saved to buy a small farm, one or both of the spouses often continue working full- or part-time to provide additional financial resources for the farm.

Another potentially viable financing alternative is for experienced and financially established farmers to loan their wisdom and capital of maturity to a younger new farmer and borrow their energy and enthusiasm. I know of a dairy farmer in Indiana, for example, who chose a full-time employee to milk his cows, with the specific intention of making it possible for the employee to buy into his farming operation. A formal commitment was not made until both families had a few years of experience to ensure that the arrangement would be a “good fit” for all concerned. He said it was almost like choosing new family members.

Perhaps most important, the dairy farmer realized that he had to expand the size of the dairy operation during the transition. The original farmer had to make it possible for the new family to make enough money from the farm to buy the farm, while the original farmer is still making a living for his family from the same farm. As the new family pays off more of the farm, the original family can continue supplementing their declining farm income and build up a retirement fund that will allow them to phase down and retire from the farming operation. Once the transition is complete, the farm can then shrink back to its “normal right size,” since it will only have to support one family.

Reference: Ikerd, John. “Financial Management on New Farms.” *University of Missouri*. 05 March 2008. [http://web.missouri.edu/~ikerdj/papers/SFT-New%20Farm%20Finance%20\(7-07\).htm](http://web.missouri.edu/~ikerdj/papers/SFT-New%20Farm%20Finance%20(7-07).htm)

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Small Farms Research Center Background. The Small Farms Research Center was developed to assist small farmers with limited resources in Alabama’s underserved communities. The center was first developed in 2000 to assist minorities, especially women, African Americans and underserved individuals improve their farm management practices, given ones condition and resources. The mission of the Center and the Small Farmers Outreach program is to assist all small and limited resources farms effectively deal with risk management and food safety issues and provide them with informational sessions. The Center has also expanded its outreach efforts to meet the needs of entrepreneurs and businessman. The center is located at Alabama A&M University in the Dawson Building. The center specializes in following areas

- Marketing and Business Plans
- Identify alternative enterprises
- Legal Issues
- International Business and Procurement
- Taxes
- Conducting seminars on Government programs and other issues
- Record keeping and Loan Application
- Personal Management
- Finances
- Accounting Issues
- Business Development

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