

What were they thinking?!?

What goes into a loan decision

Lacy Roberts, Farm Loan Manager

Farm Service Agency



What does the bank look at?

- 5 Cs of Credit
 - Character
 - Credit
 - Capacity
 - Cash Flow
 - Collateral

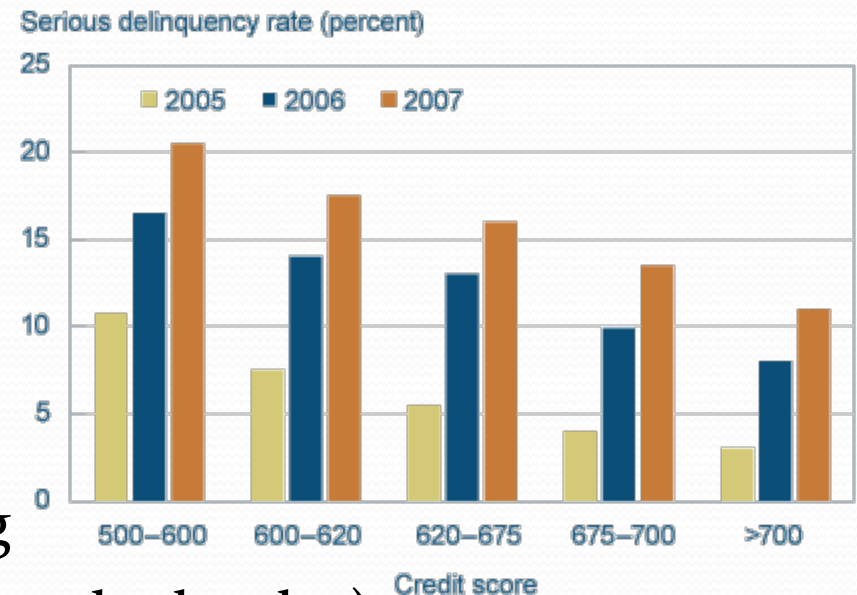


Character and Credit

- **Character** goes hand in hand with **Credit**
 - Credit History
 - Reputation in the community
 - Tell the truth
 - Past payment history with the bank
 - Real estate taxes & Income taxes paid
 - Amount of trade accounts around town (THINK: 18% interest)
- **Credit** = borrowing capacity
 - Have you maxed out every resource available? Not a good sign - potentially

Closer look at Credit History

- Credit Scores
 - 800 and Above – Golden
 - 700-800 – Good
 - 600-700 – Marginal
 - 500-600 – Poor
 - Less than 500 – Devastating
 - 0 – Awesome! (Depending on the lender)
- FSA does not base decision on credit score but on the content of your credit report



What goes into the score?

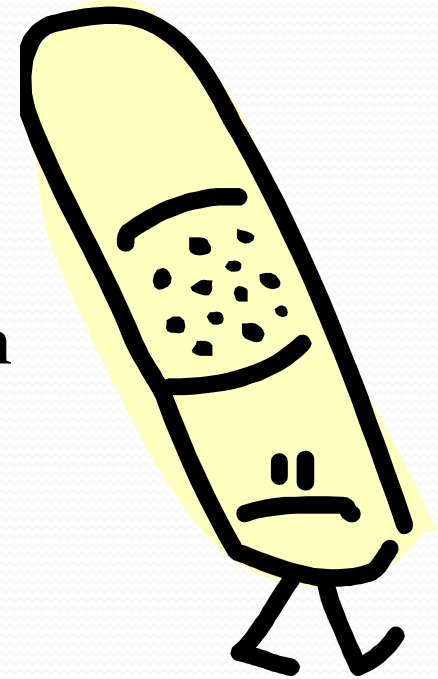
- Payment History – 35%
- Amount Owed – 30%
- Length of Credit History – 15%
- How much new credit – 10%
- Type of credit – 10%



Source: *Credit Scores & Credit Reports. How the System Really Works, What You Can Do*, by Evan Hendricks, 2005. Privacy Times, Inc.

How do you repair that?

- Get the collections paid
- Report items that are incorrect
- Order credit reports often to check
- May want to look at Identify protection
- Pay your bills on time!
- Number of Accounts that are open
- Most items stay for seven years
- Credit history is the number one reason we can't make a loan



Capacity

- The ability to repay debt – Past, Present, Future
- Timing of repayment
 - Make sure you pick a good time for a payment
- Probability of success
- Will analyze to see if have good:
 - Past management history, records, market opportunities

"You can make a small fortune in farming - provided you start with a large one."

- Anonymous

Cash Flow

- Nuts and bolts of modern lending
- Are you going to be able to pay it back?
- Are there alternative payment sources if Plan A doesn't work?
- Consider all inflows and outflows
- Will analyze Cash Flow Projection
- This may or may not be a picture of the profitability of the operation.



Developing a Projection

- Use accurate and realistic numbers
 - Know exactly how many cows you have
 - What crops are you seeding and how many acres
- Base projections on a realistic price
 - \$1.35/lb. for calves and \$4/bu wheat – can you do it?
- Consider future expansion needs
 - Newer equipment
 - Better facilities
 - How to maintain or grow herd size

Projecting Expenses

- Take a look at your last 3-5 years of expenses
- Expanding operation?
 - Look at per head cost of current operation
 - What is variable vs. fixed expense
 - Variable – Feed, vet, AUM leases, chemical, fertilizer
 - Fixed – Real estate taxes, living
 - Variable/Fixed – fuel, cash leases
- New operator?
 - Talk to several neighbors or your banker for thoughts
 - 2 ton of hay per cow x \$125/ton delivered
 - \$15-20/hd vet expense

	2011	2012	2013	2014	2015	3 yr. avg.	2016 Proj.
Crop Sales	\$ 20,000.00	\$ 60,000.00	\$ 100,000.00	\$ 100,000.00	\$ 50,000.00	\$ 83,333	
Livestock Sales	\$ 15,000.00	\$ 200,000.00	\$ 500,000.00	\$ 500,000.00	\$ 200,000.00	\$ 400,000	
Custom Hire	\$ 5,000.00	\$ 10,000.00	\$ 80,000.00	\$ 150,000.00	\$ 10,000.00	\$ 80,000	
Crop Insurance	\$ -	\$ -	\$ 1,000,000.00	\$ 150,000.00	\$ 200,000.00	\$ 450,000	
Ag Program Payments	\$ 5,000.00	\$ 5,000.00	\$ 40,000.00	\$ 3,000.00	\$ 3,000.00	\$ 15,333	
Other Income	\$ 2,000.00	\$ 2,500.00	\$ 5,000.00	\$ 2,500.00	\$ 1,000.00	\$ 2,833	
TOTAL Income:	\$ 47,000.00	\$ 277,500.00	\$ 1,725,000.00	\$ 905,500.00	\$ 464,000.00	\$ 1,031,500	
Car and Truck	\$ 1,500.00	\$ 2,000.00	\$ 2,500.00	\$ 2,500.00	\$ 30,000.00	\$ 11,667	
Chemical	\$ 10,000.00	\$ 15,000.00	\$ 35,000.00	\$ 70,000.00	\$ 50,000.00	\$ 51,667	
Custom Hire	\$ 5,000.00	\$ 30,000.00	\$ 50,000.00	\$ 5,000.00	\$ 5,000.00	\$ 20,000	
Hay, Feed, Supplement	\$ 10,000.00	\$ 30,000.00	\$ 40,000.00	\$ 50,000.00	\$ 70,000.00	\$ 53,333	
Fertilizer	\$ 10,000.00	\$ 15,000.00	\$ 70,000.00	\$ 130,000.00	\$ 50,000.00	\$ 83,333	
Fuel/Oil/Gas	\$ 20,000.00	\$ 30,000.00	\$ 70,000.00	\$ 10,000.00	\$ 50,000.00	\$ 43,333	
Interest - AOL	\$ 2,000.00	\$ 3,000.00	\$ 5,000.00	\$ 5,000.00	\$ 5,000.00	\$ 5,000	
Labor Hired	\$ 1,500.00	\$ 2,000.00	\$ 2,500.00	\$ 2,500.00	\$ 30,000.00	\$ 11,667	
Land Rent	\$ 10,000.00	\$ 15,000.00	\$ 35,000.00	\$ 70,000.00	\$ 50,000.00	\$ 51,667	
Repairs	\$ 2,000.00	\$ 4,000.00	\$ 50,000.00	\$ 40,000.00	\$ 60,000.00	\$ 50,000	
Supplies	\$ 2,000.00	\$ 4,000.00	\$ 6,000.00	\$ 6,000.00	\$ 7,000.00	\$ 6,333	
Vet/Breeding/Med.	\$ 500.00	\$ 1,500.00	\$ 3,000.00	\$ 3,500.00	\$ 5,000.00	\$ 3,833	
Other Exp	\$ 500.00	\$ 500.00	\$ 1,500.00	\$ 1,500.00	\$ 3,000.00	\$ 2,000	
Total Expenses:	\$ 75,000.00	\$ 152,000.00	\$ 370,500.00	\$ 396,000.00	\$ 415,000.00	\$ 393,833.33	
Non-Farm Income:	\$ 50,000.00	\$ 40,000.00	\$ 40,000.00	\$ -	\$ -	\$ 13,333	
Owner Withdrawal:	\$ 15,000.00	\$ 15,000.00	\$ 30,000.00	\$ 50,000.00	\$ 75,000.00	\$ 51,667	
Term Debt Payments:	\$ 5,000.00	\$ 15,000.00	\$ 70,000.00	\$ 150,000.00	\$ 200,000.00	\$ 140,000	

Collateral

- What can you pledge for the loan?
- Consider age and longevity of security
- Dirt is often the preferred collateral
- Analyze Financial Statement



Financial Statement

- Snapshot of where you are today
- Assets
 - Current
 - Intermediate
 - Long Term
- Liabilities
 - Current
 - Intermediate
 - Long Term
- Determines equity position

Lacy ~Roberts 1		Balance Sheet	
		01/01/2013 - 2013 Balance Sheet	
<u>Current Assets</u>	<u>Value</u>	<u>Current Liabilities</u>	<u>Value</u>
Cash & Equivalents	15,000	Accounts Payable	43,000
Accounts Receivable	33,000	Real Estate Taxes Payable	1,500
Crop Inventory	97,000	Cur. Portion Term Debt - FSA	19,823
Growing Crops	10,000	Cur. Portion Term Debt - Other	24,253
Market Livestock & Poultry	14,883	Accrued Interest	3,010
Prepaid Expenses & Supplies	7,000		
Total Current Assets	176,863	Total Current Liabilities	91,386
<u>Intermediate Assets</u>		<u>Intermediate Liabilities</u>	
Machinery & Equipment	140,000	Intermediate Term Debt - FSA	86,189
Farm Vehicles	95,000	Intermediate Term Debt - Other	44,221
Raised Breeding Stock	383,000		
Total Intermediate Assets	618,000	Total Intermediate Liabilities	130,410
<u>Long Term Assets</u>		<u>Long Term Liabilities</u>	
Real Estate - Land	750,000	Long Term Debt - FSA	294,188
		Long Term Debt - Other	296,526
Total Long Term Assets	750,000	Total Long Term Liabilities	590,714
TOTAL ASSETS	1,544,863	TOTAL LIABILITIES	812,510
		TOTAL EQUITY	732,353

Developing a Balance Sheet

- Use realistic valuations
- Remember it is a “snapshot in time” not a cash flow projection
- Show ALL assets and liabilities

Financial Statement, XYZ Farm

01/01/2015

Current Assets:	Current Liabilities:
Intermediate Assets:	Intermediate Liabilities :
Long Term Assets:	Long Term Liabilities :

$$\text{EQUITY} = \text{Total Assets} - \text{Total Liabilities}$$

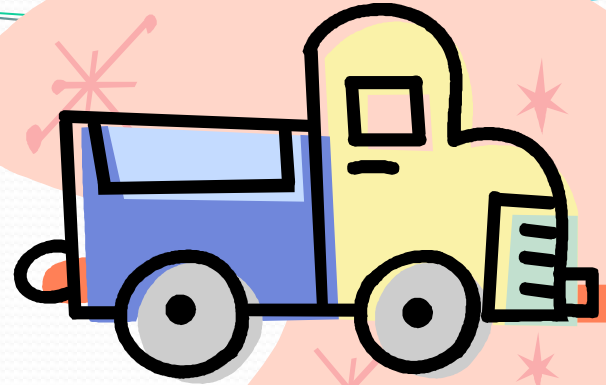
What are they?

- Lame cow out back
- Annual Operating Loan
- Buildings
- Bill at BTI
- Light calves to be sold as yearlings
- Real estate taxes
- Income Taxes Payable



What are they?

- New bull purchased
- Grain Loan with FSA
- Feeding Pickup
- Fuel bought for next year
- Savings Account
- CD at BIA for holding leases
- Cow loan



What are they?

- Machinery Loan
- Cow Herd
- Tractor
- Land Loan
- Horses
- Land
- Wheat from 2002 that has sprouted a few times over



	1/1/2016	1/1/2015	1/1/2014	1/1/2013
Current Assets				
Cash	\$ (10,000.00)	\$ 20,000.00	\$ 30,000.00	\$ 100,000.00
Accounts Rec.	\$ 30,000.00	\$ 60,000.00	\$ 5,000.00	\$ -
Crop Inventory	\$ 2,500.00	\$ 30,000.00	\$ 80,000.00	\$ 60,000.00
Growing Crops	\$ -	\$ 15,000.00	\$ 50,000.00	\$ 50,000.00
Market Livestock	\$ 30,000.00	\$ 3,000.00	\$ 2,000.00	\$ 3,000.00
Prepaid Expenses	\$ -	\$ 2,000.00	\$ 5,000.00	\$ 5,000.00
Total Current Assets:	\$ 52,500.00	\$ 130,000.00	\$ 172,000.00	\$ 218,000.00
Intermediate Assets:				
Machinery and Equipment	\$ 300,000.00	\$ 600,000.00	\$ 400,000.00	\$ 200,000.00
Farm Vehicles	\$ 45,000.00	\$ 75,000.00	\$ 75,000.00	\$ 3,000.00
Raised Breeding Stock	\$ 250,000.00	\$ 350,000.00	\$ 350,000.00	\$ 300,000.00
Total Int. Assets:	\$ 595,000.00	\$ 1,025,000.00	\$ 825,000.00	\$ 503,000.00
Long Term Assets:				
Real Estate:	\$ 300,000.00	\$ 300,000.00	\$ 300,000.00	\$ 300,000.00
Total Long Term:	\$ 300,000.00	\$ 300,000.00	\$ 300,000.00	\$ 300,000.00
Total Assets:	\$ 947,500.00	\$ 1,455,000.00	\$ 1,297,000.00	\$ 1,021,000.00
Current Liabilities:				
Accounts Payable	\$ 150,000.00	\$ 40,000.00	\$ 10,000.00	\$ -
Line of Credit - Bank	\$ 150,000.00	\$ 30,000.00	\$ 100,000.00	\$ 40,000.00
Real Estate Taxes Payable:	\$ 3,000.00	\$ 1,000.00	\$ -	\$ -
Current Portion of Debt Payment:	\$ 70,000.00	\$ 50,000.00	\$ 50,000.00	\$ 10,000.00
Accrued Interest:	\$ 20,000.00	\$ 3,000.00	\$ 1,500.00	\$ 1,500.00
Total Current Liabilities:	\$ 393,000.00	\$ 124,000.00	\$ 161,500.00	\$ 51,500.00
Total Int. Liabilities:	\$ 400,000.00	\$ 500,000.00	\$ 600,000.00	\$ 550,000.00
Long Term Debt:	\$ 150,000.00	\$ 170,000.00	\$ 190,000.00	\$ 250,000.00
Total Liabilities:	\$ 943,000.00	\$ 794,000.00	\$ 951,500.00	\$ 851,500.00
Total Equity:	\$ 4,500.00	\$ 661,000.00	\$ 345,500.00	\$ 169,500.00

What does it tell me?

- Liquidity: Can I make my payments now and in the future?
 - Current Ratio: $\text{Current Assets} / \text{Current Liabilities}$
 - Target Range: At least 1:1
 - Working Capital: $\text{Current Assets} - \text{Current Liabilities}$
- Solvency: If I had to sell out, could I pay everything off?
 - Equity = $\text{Total Assets} - \text{Total Liabilities}$
 - Target Ratio: Greater than 0
 - Debt/Asset Ratio: $\text{Total Liabilities} / \text{Total Assets}$
 - Target Ratio: 50% or less

What does it tell me?

- Debt/cow
 - Total debt/number of cows
 - Target Ratio: Less than the cow is worth.
- Machinery/acres
 - Total Valuation of machinery/# of acres covered
 - Target Ratio: \$400/acre or less



How well are you taking care of your collateral?

- Cows and Crops
 - What is the condition of the livestock?
 - Are the fields clean and well taken care of?
 - What has been your past history of production?



What do I need?

- A PLAN!!!
 - SWOT Analysis
 - Strengths
 - Weakness
 - Opportunities
 - Threats
- Financial Statement
- Cash Flow Projection
- Any Past History
- Be Ready to Address the 5c's

*“Farming looks mighty easy when your plow is a pencil and you're a thousand miles from the corn field.”
- Dwight D. Eisenhower*

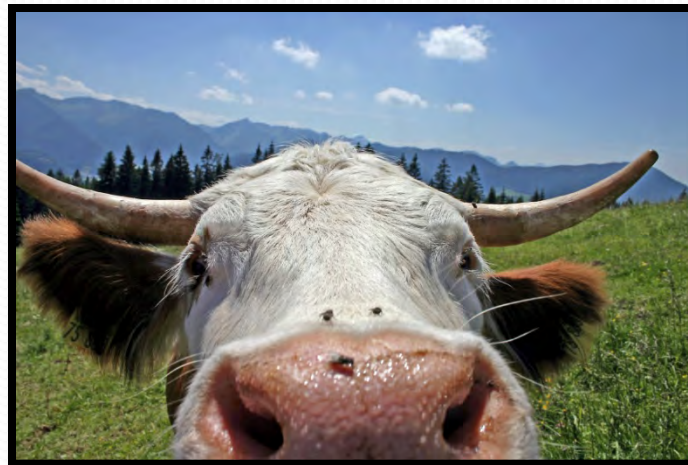
Remember:

- If done properly:

"Agriculture is our wisest pursuit, because it will, in the end, contribute most to real wealth, good morals, and happiness."

- Letter from Thomas Jefferson to George Washington (1787)

- Always make sure you have an end goal in mind and what your exit strategy is



Questions?

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