Financial Management on New Farms

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Many bright, energetic young people today would gladly choose farming as their occupation, if they could just find some way to get started. I have met dozens of these would-be “new farmers” over the past few years, at sustainable agricultural conferences and on college campuses all across the United States and Canada. If they could get the money to buy some land and a few tools, they would become farmers; but many of them can't. Established farmers, if they are viewed by lenders as anything other than conventional farmers, face many of the same frustrations when they want to change or expand their operations.

On the other hand, it's fairly easy for a conventional farmer to borrow money for new ventures, such as expanding acreages of cropland or building a new confinement livestock facility. This is particularly true during time of profitable commodity prices. Even government subsidized loans for beginning farmers tend to go to young farmers who want to grow conventional farm commodities for traditional markets. Lenders understand this kind of farming. Most don't understand the new sustainable farming operations, and thus aren't willing to lend them money.

It takes money to run a business, even a “new-farm” business. However, as my younger brother advises, “when you hear someone say ‘it takes money to make money', always ask yourself; ‘what is he or she trying to sell you?'” My brother managed to make a good living on a small family dairy farm for more than 40-years, by saving money rather than spending money. Honestly, I have known a lot more farmers who got into financial problems because they borrowed too much money than because they borrowed too little. Conventional industrial farmers have to borrow money; they have to expand as fast as they can to survive. New farmers, however, should give a good bit of thought to how much money they really need.

The new sustainable farm must be managed as a living organization. Living organizations, like living organisms, have a natural, healthy rate of growth and a natural, healthy mature size. Growing too fast or growing too large is neither healthy nor sustainable. Living organizations, like living organisms, need to be nurtured into life and nurtured during their early stages of development, until they reach maturity. Mature living organizations, like mature living organisms, acquire the natural capacity to grow from within; they are self-renewing and regenerative. At maturity, they are also able to produce more than they need for themselves; they are able to reproduce and to nurture others. Financing the new farm is like nurturing a living thing, supplementing it financially during natural times of deficit or need and taking from it financially during times of plenty – when it is capable of producing more than enough to sustain itself.

Conventional financial management focuses on financial statistics, such as liquidity, solvency, and financial risks. Liquidity deals with cash flow; how much money do you expect to have coming in and going out during specific times of the year? Will the accumulated inflow meet the necessary outflow during all times of the year? Solvency deals with questions of how much you owe relative to how much you own today, whether you could sell out and expect to pay off all of your debts, if necessary. Financial risk relates to the odds or chances that you might be caught in a situation in the future with too much debt and too little equity, and thus not be able to pay off your debts.

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.

They don't understand how a new farmer can expect to realize greater economic returns without expanding the scale or size of their farming operation. If they loan money to these new kinds of farmers, they don't know how to estimate whether they will be able to meet their repayment schedules. If they loan much money to a farmer who owns very little land, they are afraid of ending up with a loan greater than the value of the farm. The financial risks seem too great. It is going to take a long time for commercial lenders to gain enough understanding and confidence in these new ways of farming to treat new farmers and conventional farmers alike, particularly given their current bias in thinking that farms must get bigger faster in order to survive.

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.

Various “farm link” programs have been initiated around the country to help retiring farmers who want to keep their land in farming to link up with potential new farmers. However, such programs typically require some special arrangement or concession on the part of the retiring farmer to be successful. The Carrot Project, a northeastern nonprofit organization, provides loans and loan guarantees to farmers who want to start sustainable farming operations. Some local credit unions have also encouraged established farmers to set aside funds in retirement accounts that could be used to help beginning farmers. However, regenerating and renewing the farms and farmers needed to ensure a sustainable agriculture remains a major challenge. Like everything else about this new way of farming, financial management requires more imagination, creativity, and tenacity.