Understanding the Food Production Sector

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Understanding the Food Production Sector

Introduction

This chapter provides an overview of the food production sector and the direct role CDFIs have in supporting this sector. Food production means "on the ground" production of crops, livestock, and livestock products such as milk and eggs. Many food producers also make processed items such as cheeses, cured meats, and sauce. This type of production, on a farm, is commonly referred to as value-added. In this chapter, we provide a framework for understanding the small scale agriculture sector, its producers including on-farm value-added, as well as its unique attributes. The sections include:

- The Status of Emerging Agriculture and Changes in the Sector
- Understanding the Small/Emerging Agricultural Sector
- CDFI Self-Assessment – Entering the Food Production Sector
- Market Analysis and Outreach for TA Resources
- Technical Assistance – Developing Best Practices
- The Call for CDFIs to Engage

The goal of this chapter is to provide a foundation for a CDFI or other lenders to have a solid overview of the attributes of the food production sector, to determine its appropriate role in supporting this sector, and to develop an effective and viable program which fits its own programmatic goals.

I. The State of Emerging Agriculture

In the 20th century, agriculture in the United States underwent a radical transformation. It changed from an industry represented by many small family owned and operated farms that produced food and fiber for both domestic use and export, to an industry where farms became increasingly large focused on a single crop or animal. This transformation of the farms was supported by a change in government policies and infrastructure that favored the largest farms and the production of commodities. This shift led to the creation of huge farm properties in geographically suitable regions like California and the Mid-West. This increased food production and lowered costs but has also made it more difficult for a small to mid scale farmer to compete financially, and has diminished the farming activities in areas of the country which do not have the geographic features necessary to farm at the agri-business scale.

In discussions related to food and agriculture, the word 'commodity' can be used in two different ways. First, it may refer to specific crops supported by federal "commodity crop" program subsidy such as peanuts, cotton, corn, and soybeans where the product is produced on an agri-business scale and sold in bulk. Second, it may refer to a smaller system where one product is not differentiated from other like products in the market, such as tomatoes, potatoes, or apples. These commodity products do not have unique attributes to generate a price difference (like an heirloom tomato, fingerling potatoes, or a Jonamac apple), and the farmer producing the products cannot dictate pricing or develop specialized sales outlets. The commodity products in this latter category (smaller scale but not specialized) may not qualify or fall under federal subsidy programs or other federal government supports, which are geared to the agri-business commodity crop. Comprehension of these factors is important to developing an understanding of the food production sector.

While agriculture has been a major economic driver in the United States since the country's founding, agriculture is again undergoing a fundamental transition as large scale commodity agribusiness is being augmented, and in some cases supplanted by, smaller scale farms producing foods for domestic and local consumption. There are many factors driving this shift, including concerns about food safety, carbon footprint, genetic food engineering, and food preservation methods, as well as an increasing interest in and awareness of the nutritional qualities of foods, the need to eat more fruits and vegetables, the desire to know where food comes from, and a commitment to preserving family farms. All of these factors directly benefit the small and emerging farm sector. These contributing factors have created a highly dynamic situation for emerging farm enterprises as they encounter increasing demand for product, but are financially constrained due to limited loan capital and fragmented technical assistance resources. In spite of the challenge, smaller farms are responding to increasing market demand for healthier, fresh products grown locally, and are demonstrating economic viability. In short, they are starting to fill a vital role in producing high quality foods which meet local and regional demand at a reasonable cost, can reach into urban settings, and are revitalizing an economic engine of growth through an expanded local food supply chain.

As interest in locally produced food has been increasing in the past decade, there has been a significant increase in the number and product range of small farms across the country. The number of US farms smaller than 49 acres grew 15% from 1997-2007 (USDA 2007 Agriculture Census), and increased 4% as a portion of total farms. For census-based information on number and size of farms please see the USDA's National Agricultural Statistic Service website: http://www.agcensus.usda.gov/.

Likewise, in the past decade there has been a significant increase in the number of farmers' markets attended by nearby farms. Once considered a novelty, they have become embedded in both urban and rural settings and have grown significantly in range of products and scale. More recently, community supported agriculture (CSA) has gone from a specialized way of sourcing high quality local foods to a well known and broadly accepted way for more casual consumers to have local produce brought to them through work, social and home settings. The idea of buying a share or part share in a CSA has become mainstream in many urban settings, where food is delivered to entire office buildings. Organic foods have gained mainstream acceptance, with major food chains having their own line of organic products. Consumer desire for high quality, high nutrition, and less processed foods is actively demonstrated in the rapid acceptance of what would have been a niche product only years ago, such as Greek yogurt, vegan foods, and gluten free foods. In short, the food market has shifted dramatically in only the past ten years, with much higher expectations for food quality, and significant increase in interest in how foods are produced or processed and where they were grown, and a specific desire to support product grown locally.

This trend is the reason for the concurrent growth in the food production sector. People who produced food items on a casual basis are expanding into small scale businesses; and hobby farms are becoming full time endeavors. Farms are expanding from sales to farmers markets and local retail outlets to larger scale endeavors including selling to food hubs and distributors with strict quantity and quality guidelines. Restaurants are increasingly defining their menus around locally produced items, and the "locavore" movement has become virtually mainstream across the country. Over the past several years, the small farming niche has evolved to be a more broadly accepted element of consumer and commercial society. There has been parallel growth in the support systems around the sector such as food hubs, commercial kitchens, and food processing facilities, as well as development of agri-tourism and other food focused regional or topical activities.

Despite the growth and development of this sector, there are several critical obstacles to it achieving its full potential.

For the farming side, there are key characteristics which make it difficult to obtain financing, such as:

- Lack of capital or an established equity base (limited financial cushion or fallback).
- Lack of familiarity with business planning tools, and the capability and technical skill to convert farm production plans to cash flow projections.
- Poor credit histories or lack of well-established credit historiesLack of secondary sources of income sufficient to support the requested debt.

From the lending side, there are factors which limit the appeal of lending into this sector:

- Lending activity has diminished to perceived higher risk sectors with unproven track records or that are non-conforming to industry standards.
- Agriculture lending has always been a specialized field; fewer commercial and community banks have the in-house expertise and industry resources to readily lend into the sector.
- Lending into this sector has historically relied on credit supports such as production contracts, crop insurance, and guaranty programs. These are not typically available to small farms, and small farms are often striving for a diverse crop or product mix which does not fit with a commodity production contract.
- Loans to small and emerging farms are often in small dollar amounts ($50,000 or less) and may require flexible repayment based on crop/product development and sales cycles. These loan sizes and repayment structures do not fit in a traditional small business banking model.
- Agricultural federal and state guarantee programs may not be available to CDFIs, or may be more difficult for CDFIs to demonstrate eligibility, such as the Farm Service Agency guaranteed loan program.
- Subordinate financing arrangements which may be available through economic development agencies in order to induce commercial and community banks to make the senior loan are often not readily available to agricultural endeavors.

In addition, agricultural banks (specializing in agricultural lending) have been highly stressed:

- By the third quarter of 2010, one in fifty loans (1.9%) of all types at agricultural banks was delinquent — higher than any level in two decades.
- Between 2008 and 2010, there were 15 agricultural bank failures, more than in the previous 15 years combined.

While the future of increased agricultural activity through a network of localized farm ventures is of heightened importance and interest, the associated need for loan capital is not being met. Community and commercial banks are unlikely to enter a sector which requires specialized knowledge, has non-standard repayment terms, and does not have widespread credit supports to mitigate the risk. Nevertheless, the need for financing is clear, and it is alternative lenders such as CDFIs who can fill the gap and can potentially pave the way for conventional lenders to re-learn specialized industry knowledge and reestablish comfort with and confidence in this sector.

CDFI's can bring critical resources to this sector by:

- Development of an active network of accessible and qualified technical assistance (TA) resources which provide business guidance such as financial modeling, legal advice and marketing, as well as product-specific agricultural knowledge; and
- Financial supports including financial counseling, direct lending, and partnership lending with other organizations such as banks, other lending organizations, foundations, etc., to increase access to funding opportunities and ensure that borrowers enter into appropriate financial arrangements.

CDFIs are perfectly positioned to support small and medium-sized farms because they understand lending approaches intrinsic to economic development.

II. Understanding the Small and Emerging Farm Sector

It is important in this sector to understand the spectrum of entities and structures which will be encountered. Agricultural borrowers can be broadly classified into four groups:

- Refugee/Immigrant.
- Small Part-time.
- Small Full Time.
- Commercial.

Loan applicants will usually fit into one of these groups and may be described by the factors outlined in each of five categories: 1) General Characteristics, 2) Challenges, 3) Financing Needs, 4) Key Risk Factors, and 5) Analysis Ratios *(see appendix I)*. Some applicants will show characteristics across two or more groups. Specific lending programs can be designed around these categories, often with highly specialized TA providers and partners; or a CDFI can work directly with borrowers and build necessary capacity around the borrower's broader TA needs.

For some borrowers, the goal is to move along the spectrum to become a larger, financially independent and viable farm. Some successful borrowers will remain within the original niche, using the business as a sideline for personal benefit and additional financial return. The CDFI needs to recognize and support the applicant in his/her current situation, as well as to recognize what his/her goal is for growth, as the associated structural and financial needs will vary accordingly.

Know Your Farmer:
Small-Mid Scale Agriculture Characteristics

There are different characteristics which are typical of certain sizes and types of farmers and farming entities. These are not exhaustive, but provide a framework for understanding the practical situation of the farm that the CDFI is dealing with, as well as the critical needs of lending and providing TA support for that entity. *See appendix I for a broad overview of these characteristics.*

Understanding where an applicant is within the above spectrum creates a strong baseline for working with a borrower. However, within this sector there are no "standard" farming models. As a result, each farm application needs to be looked at diligently to understand not only its core products but also its aggregated product mix, cash flow, seasonality, and capital requirements. This sector can be challenging for CDFIs to understand in both its simplicity and complexity.

Know Your Products:

Small Farm Complexity and Diversity

The simplicity of looking at a single, small scale farm enterprise is that it seems very intuitive, and the risks seem clear. But as the CDFI deals with actual farming loan applications, there are many factors which create significant complexity and diversity, and make the seemingly basic analysis a much more challenging process. This section describes four increasingly complex farm ventures whose characteristics are representative of typical applicants that must be integrated into any lending and TA assessment.

Simple Farm Model:

If the farm is growing a variety of seasonal vegetables and selling retail, for example through Community Supported Agriculture (CSA), the business model seems simple: buy plants and supplies in the spring (cash outflow); collect payments from CSA members in the spring and summer (cash inflow); and provide product on a periodic basis from summer through fall. There is a fairly simple model of cash out in the spring, reduced by CSA payments, and then likely augmented by supplemental product sales that bolster cash flow in the fall and allow full loan repayment. The lending decision in terms of needed funds and appropriate repayment schedule is easy to define. However, add in crop issues such as disease, weather, insect damage, or soil fertility, and the model changes. There may be a greater need for cash than anticipated, and/or reduced overall revenues, which impacts the borrower's ability to repay the loan within the loan's terms. This can occur even with proper farm management and all appropriate precautions taken. It is imperative to address all the crops produced to understand the entire production spectrum and associated potential and risk.

Somewhat Complex Farm Model:

The simple seasonal vegetable model is made more complex by the farmer's desire to make the business more efficient and productive by adding amenities such as storage sheds, hoop houses, or irrigation systems to extend the season and levels of production. This type of farm is likely to need a multi-year loan instead of a single season loan. Add in poultry for egg sales, and the farm has a more consistent product delivery model year around which stabilizes cash flow and lowers risk. If a farmer has egg layers, adding poultry for meat sale is an obvious next step. This results in a different production cycle, the logistics of slaughter and butchering, and increased food safety regulations, but also creates a shelf stable product (if frozen) which reduces the need for seasonal sale and the risk of spoilage or waste. If the poultry is turkey, in particular, the farmer now has a highly seasonal poultry sale (October through December) with high profit potential, but a need for strong marketing and product delivery mechanisms; a concurrent need for timely butchering; and limited ability to freeze and store for timely resale if processing resources are not already in place.

The simple concept and the easily understood individual products can rapidly develop into a more complex model where each aspect has its own inherent requirements, attributes and risks. More complexity may be found with the addition of a different type of growth product altogether: say mushrooms, which have a very short growth cycle but require highly specialized production skills and different marketing constraints; fruit or nut trees which require access to or development of a mature orchard, which can take 7-10 years and whose short and intense harvesting cycle may coincide with other crop cycles; or maple sugaring which requires not only access to a mature sugar stand, but also the infrastructure to tap the trees, and boil down and process the sap into syrup.

Understanding the individual crops and/or products, as well as infrastructure requirements and the cash flow timelines which overlap based on production and sale is necessary to assessing potential opportunities, risks and overall viability of the farm business.

Increasingly Complex - Marketing Requirements for a Small Farm Model:
Once the farmer has a product, how well does he or she get to market? Does he or she sell wholesale in bulk, or to restaurants, which have well known cash flow characteristics? Do they sell to farmers' markets or CSAs, which are accessible but cost intensive to deliver into versus other sales outlets? Or do they do business with institutional buyers, who have stable and defined demand but require timely delivery of agreed upon amounts and products? Is there a need for an approved and certified commercial kitchen for processing, or is processing outsourced? Is there a need for bar coding for retail sales? The complexity of marketing requirements increases with each additional product. It requires more agricultural and managerial skill, can increase the capital requirements for marketing, and may require more structured and reliable methods of getting product to market. However, each additional product and sales outlet increases the diversity and reduces the overall risk of the farm.

Overall Complexity and Diversity:
An effective lender understands each major product cycle and how it affects cash flow individually. The lender is able to overlay each product cycle in the farm's enterprise model to understand the aggregation of cash flow, of customers, and of the risks in the enterprise. Increased diversity on a farm reduces the reliance on a single crop or product which may in turn reduce risk, but that diversity requires more developed business and managerial skills including marketing, human resources, technical farming knowledge, financial reporting and the like. It is critical that organizations such as CDFIs entering this sector understand the complexity of a small farm enterprise, can break its operation into specific cash flow components, can assess its business management as well as agri-business needs, and are able to bring the financial and TA resources to the table to foster success.

III. CDFI Self-Assessment – Entering the Food Production Sector *(see Appendix II)*

A CDFI self-assessment to consider the commitment of resources into this sector, can guide decision making by identifiying a pathway to establish the internal and external resources needed to succeed. As explained in Section II, this is not a sector that has a standard type of borrower, a typical loan structure, or easily defined risk. However, a CDFI may find that several types of enterprises are more common in their specific area. Completing a thorough evaluation of the CDFI's target market, as well as the financial and industry expertise needed are critical in establishing a lending and TA program. The Self-Assessment Tool, in appendix II, is explained in detail below and can be used to help guide the decision to enter the agriculture sector.

There are no right or wrong answers. However, the answers to the self-assessment will place a CDFI somewhere along the spectrum of sector engagement, in terms of priority, capacity, and market. This is extremely beneficial to identify and understand before committing time and resources to agriculture sector lending.

Mission Alignment and Strategic Priority (see appendix II)

The very first question to ask is if engagement in the agriculture sector is closely aligned with the mission and goals of the CDFI. The answer could very well be a deal breaker and requires candor and self reflection. Clearly, there is a lot of interest in the local foods movement nationally—in the media, in the markets, and amongst funders. The question is, where does the CDFI fit into the mix? Is incorporating agricultural lending aligned with the organization's current focus, or would it require rethinking the core mission and operations of the organization? Would the CDFI be better served to focus on a subset of the sector—such as farm worker housing, if the CDFI focuses on housing; or farm co-op development, if the CDFI specializes in cooperatives? Some CDFIs may choose to focus on the food supply chain—one step removed from farm production—because that is where job creation lies which is core to mission; other CDFIs might focus on farm to school efforts because its target audience is children. The key is to determine where in the industry it makes sense for the CDFI to engage, and therefore have the most impact.

If the agriculture sector aligns with CDFI mission, it should be determined if it is, or could become, a strategic priority. Building agricultural lending capacity in house, and the technical assistance components necessary to support it, will require time and commitment from existing staff, unless new staff are hired. Board support, as well as buy-in from staff, is paramount to creating a quality program with effective lending into the sector.

The self-assessment starts with the question of whether or not lending in the agriculture sector is a priority for the organization, because it is one of the most important to answer affirmatively. However, it may be the last question that can be answered, because completing the entire self assessment will give the CDFI a comprehensive picture of its ability to engage in agriculture sector lending.

Market Analysis—The Landscape (see appendix II)

This section of the self-assessment encourages the CDFI to complete a broad based market analysis in order to determine what role the organization can and should fill in supporting agricultural development. This includes identification of and contact with local agricultural and skill-specific resources, potential borrowers (i.e. the farm community), lenders, and other available financial resources. The market analysis helps define what business and financial resources are currently in place, what are lacking, and therefore potential gaps the organization can fill. The market analysis also begins to build the CDFI's professional network of agricultural support services and resources, crucial to success in this sector.

There are enough inherent challenges in this sector that effective marshaling of resources, outside the organization, will make a significant difference in the program's efficacy and, more importantly, in being able to meet deliverable objectives and maintain a commitment to this sector. We encourage convening key food system stakeholders early in the process of assessing and designing a program. The following groups will be highly motivated to assist with market analysis and outreach work and should be involved at the outset, once a preliminary self assessment has been completed and a decision been made to proceed.

List of Key Stakeholders to Contact for Agricultural Lending and/or Technical Assistance Program				
State Department of Agriculture staff	University Cooperative Extension System Agents	USDA Rural Development and Farm Service Agency Staff	State agriculture producer/trade groups	Public, private/non-profit agricultural advocacy and advancement organizations
Agricultural lenders—local, regional	Community Development Corporations and Financial Institutions	Independent agricultural consultants	Farmers – Local	Farmers – out of region but in same products as local farmers

Once the CDFI has identified all relevant agriculture sector stakeholders, the focus should shift to identification of target borrowers. For example, will the CDFI lend to:

- Refugee and immigrant programs?
- Small scale farms that sell through farmers markets?
- Farms with specialty products like mushrooms, maple syrup, grass fed beef, or a combination thereof?
- Established farms that need to expand products and land-use to increase diversity and reduce cash flow seasonality?

Identifying the niche that the organization is best suited to serve is important, because a better understanding of the components of that niche, and improved resource connections to support it, can increase the effectiveness of marketing and lending efforts.

At the same time, measure the niche against potential demand for the CDFI's lending services—i.e. if it is too small, a CDFI may find that it has loan funds and no applications. However, making it too broad and taking on all applicants may make it difficult to be effective and more challenging to deal with the normal variables of any business model.

Understanding the local or regional landscape allows the CDFI to evaluate which market will best fit its lending platform. It will also help prioritize lending opportunities into a defined niche and establish program parameters. In particular, having a good knowledge base will give confidence to the board approving a commitment of resources, as well as assist in educating a loan committee tasked with reviewing actual financing proposals.

Internal Capacity and Financial Analysis (see appendix II)

It is critical for the CDFI to identify its internal capacity to lend into the agriculture sector and determine ways to build that capacity if lacking. This section of the self assessment outlines how to create a clear blueprint for an organization to identify financial and resource commitments, set timelines and expectations.

This will include defining:
- Approval processes and decision makers.
- Internal resources for outreach and for assessing applicants.
- Internal resources for loan management.
- An appropriate pool of capital in terms of risk tolerance and dollar size.
- Type of loan products offered.
- A list of resources and what each resource can realistically provide.
- An appropriate and clearly defined timeline to make financing investments and to assess outcomes.

The complexity of the target borrower will dictate the resource needs and the timelines, making it crucial to assess the market need and the organization's role in meeting that need. As with any new loan program in a complex, emerging market, hope for the best and plan for the worst in order to create the most favorable outcome for all the stakeholders.

Analyzing the results of the Self Assessment (see appendix II)

The self assessment should give a CDFI a broad understanding of its capacity to engage in the agriculture sector, should highlight both strengths and weaknesses, and give the CDFI a clear indication of specific areas that must be addressed if the sector is to become a priority of the organization. The self assessment provides baseline information—a starting point, from which to argue the case for, or against, agriculture sector involvement.

IV. Elements of an Effective Agricultural Technical Assistence and Lending Program – A Framework for Success

There are several elements and methods to deliver effective technical assistance (TA) in this sector. However, we want to emphasize that while there is additional complexity and diversity within this sector, there is often less in-house agricultural sector knowledge among lenders; and therefore appropriate and effective TA resources are critical to successful lending. Planning the TA and lending strategy, identifying appropriate resources, and aligning them with a CDFI's lending department, will significantly increase the CDFI's ability to lend into the agriculture sector.

This section outlines the components of an effective, efficient TA program for CDFIs. The structure of the program depends on many factors, including the location of the CDFI and its target audience, the unique and individualized needs of the agricultural sector in the CDFI's region, and the organizational structure of the CDFI itself. For this reason, we emphasize key elements that an agricultural TA program ideally should include, but not a strict structure for how to organize those elements. Coastal Enterprises, Inc., a CDFI in Wiscasset, Maine, chose to create an in-house agricultural TA program to target agricultural sector development work in Maine. Other CDFIs may be better-suited to collaborate with other organizations that can provide TA Program services. Regardless, the following elements are critical for success:

- *The Point Person*: This is the CDFI's direct connection to the agricultural sector in the region they serve. The point person could be a program manager or lender, but should perform all of the following functions:
  - build the pipeline of potential agricultural borrowers;
  - complete initial screening/assessment of loan applications;

- coordinate appropriate TA for potential borrowers, or current borrowers, should the need arise;
- engage with the network of agriculture-related service providers in the CDFI service area;
- understand the broader economic context and the agricultural sector's place therein;
- act often as liaison between the borrower and the lender and help to fill the 'gaps' in sector-specific knowledge for the lender (clearinghouse function).

  This position is critical. Lending expertise is not mandatory. However, as the point person operates at the intersection of agricultural business development and finance, s/he should have a working knowledge of business plan development, finance, and lending in order to effectively coordinate with staff and TA providers, to guide potential agricultural borrowers towards successful financing. It is essential that the point person is trusted within the agricultural community and is regarded as both an advocate and a resource for farmers (the same should be said for the CDFI affiliated with the point person).

- *Initial Filtering/Assessment*: The point person conducts the initial assessment of the agricultural loan application and/or agricultural business plan and determines the next step for the potential borrower. One of the challenges facing this sector is that applicants often get diverse advice from sources with varying degrees of skill, knowledge, accessibility and commitment.

  The agricultural point person can become known as the resource that gathers the disparate threads of information and organizes them for the borrower in a way that makes sense. The point person can work with the potential borrower on business plan and loan application improvements and fill in the missing information in the financial, operational, and marketing plan/strategy of the farm. This takes the burden off of the CDFI to build individual capacity in agricultural sector knowledge among lending staff as they can rely on the point person to provide the agriculture-related data.

  Ultimately, the importance of this filtering function is not just to help the organization operate efficiently, but also to help this sector as a whole operate effectively. This filtering means considering each applicant and reviewing for two things:

  1. *Are there major TA needs for business viability, before the applicant reaches loan discussion?*
     - This could include business planning, market research, marketing strategy, management structure, financial model building, obtaining appropriate land or facilities. T
     - his high-level screening will save everyone time and effort. Potential borrowers ideally should be prepared to make their best pitch. This is the stage to determine basic business development needs and refer the applicant to appropriate TA resources, ensuring timely support and strengthening the farm business plan and the loan application overall.

2. *Does the loan application and/or business plan have viability? Are the basic business requirements covered, but specialized TA needed to strengthen the business plan?*
   - Review the information to make a basic assessment about whether the farm business concept is feasible. This extends to the farm's financial resources, individual management capability, physical assets (land, buildings, equipment, etc.), ability to reach a viable market, ability to adequately report and manage cash flow, risk mitigation strategies, and similar business plan elements.
   - The type of specialized TA required will depend directly on the food production niche the applicant intends to fill. A CDFI's skills in determining the need, finding the right TA resource, and making strong referrals will have a direct impact on the success of the project both in business planning and financing.

Once the initial screening process has been completed, and the CDFI has a viable loan applicant, the point person will refer the applicant to lending staff. The point person will continue to play a strong role, as s/he likely has the broader market and sector knowledge and performs a great deal of the networking among organizations and other TA resources.

- *Agricultural Sector TA Network: Engagement and Collaboration:* An agricultural TA program is only as good as its resources, and strong professional relationships within the agriculture and business networks are absolutely vital to program success. It cannot be stressed enough that a highly collaborative, team-based approach to business planning is a crucial element of an effective agricultural TA program, and to developing viable farm business plans. A central role of the point person is to understand the TA that the potential agricultural borrower is already receiving, and then introduce appropriate additional TA provider(s) as needed.

Effective TA increases the business and financial capacity of the borrower, the strength of the farm business model overall and mitigates risk for the lender. The result should be more loans approved, with a higher degree of probability that they will be repaid. TA in this context is broadly defined as business development support, in particular business planning and business/financial management capacity building. The timing of TA is critical. The most effective TA is both proactive and preemptive: it is offered before a potential borrower even fills out a loan application and before problems arise around financing.

TA resources come in a wide variety of forms and must be tailored to the unique and specific need of farmers. Assistance includes, but is not limited to:

- business and financial planning;
- agriculture production and management expertise;
- peer expertise and hands-on advice to provide ongoing knowledge-based support;
- computer and bookkeeping skills;
- legal and regulatory guidance; and

- grant writing and identification of investment opportunities through foundations, federal agencies, and other funding sources.

Engagement among TA providers ideally should be collaborative, with the goal of assisting clients in developing robust, informed, investment-quality business plans. This sector requires constant knowledge building and expanded networking due to rapidly evolving markets and the need for real-time responses to issues that arise in any crop or livestock production cycle. Networking can also directly facilitate co-marketing or broader marketing efforts which can have a significant impact for the applicant as well as the sector in the CDFI's region.

➢ *Dedicated Agricultural Lending Staff*: A CDFI will need to invest in building agricutlure sector-specific skills within its lending staff if it intends to build its portfolio of agricultural loans. The point person can help guide and advise lenders to develop viable loan applications, and to prepare the borrower for financing. However, lender knowledge of the sector will ensure effective analysis and efficient approval processes. It is entirely possible that the point person is also a lender and can serve both functions, especially at the outset when the volume of agricultural loans is small.

V. Conclusion: The Call for CDFIs to Engage

CDFIs are well positioned to support the emerging agriculture sector in a localized market, as well as within a national network, because of their experience with the unconventional borrower. CDFIs understand the need for strong TA to help any small business reach its goals, and have a history of providing that TA, directly or through connections to strong individual TA providers. CDFIs also understand the crucial importance of creating a network of opportunity that will help a business reach its full potential by being connected with the right resources at the right time. Emerging agriculture in the U.S. currently has incredible vitality and economic potential, but its resource base is highly fragmented. Historically, farmers have passed down knowledge between generations, resulting in a limited and ever-shrinking resource pool of experience. Further, each crop and animal mix is unique to its natural and market environment, and the current pace at which the sector and market factors are evolving makes the transfer of knowledge and experience among players challenging. Finally, agriculture does not operate under a common business model like a bodega, a hair salon, or a small apartment building does. These unconventional factors demonstrate the need for the sector to share knowledge and experience to ensure that producers, entrepreneurs, and the TA resource pool have the tools that are necessary for continued growth and expansion.

The ability of CDFIs to understand these complexities and to provide hands-on support to reach improved social outcomes will make this possible. And, as CDFIs lay the groundwork toward meeting this goal, they can engage and integrate additional lending and TA resources into the development model, further expanding the network of resources dedicated to growing this industry across the country. CDFIs are critical players in creating economic opportunities both through their direct expertise, and also through their ability to lead other capital and TA resources to an area of need. The need for a healthier foods system is clear, and the capacity of CDFIs to be a catalyst in this sector holds great potential.

Appendix I

Know Your Farmer: Small – Mid Scale Agriculture Characteristics

Refugee and Immigrant Borrowers

General Characteristics
• Borrowers will require network of TA providers; e.g., refugee services, agricultural support, business training, etc. • Borrowers may operate in a cash or "informal" economy, and have limited experience with financial service providers. • … • Borrowers may have practical knowledge (farming and basic enterprise) but unlikely to understand paperwork, legal, accounting etc. • Language barriers. •
Challenges
• Generating enough income to be viable. • Developing skills needed in a structured economy (banking, record keeping, transportation). • Need for strong support network within immigrant community and technical support providers.
Financing Needs
• Micro loans ($250-$1,000). • Seasonal use, with seasonal repayment based on product's production and sale. • Loan and repayment will be in one cycle. • Correlate loan payments to cash flow. • Lender may need to accept cash payments. • Payment schedules structured around cash flow (highly seasonal). • Borrowers may not have deposit accounts;may need to borrow 100% (no equity).
Key Risk Factors
• Absence of strong partnerships with support organizations • Willingness of borrower to undertake financial skills training.
Analysis Ratios
• Cash receipts to pay loan. • Possible loan loss reserves or guarantee as part of program. • Ability to subsidize program through grants or other income sources.

Small Part-Time Borrowers

General Characteristics
• Limited capital. • Small number of products, one failure may equal disaster for the farm business. • Defined experience with one or a few products but skill is with that niche; not a diverse skill set. • May have agriculture skills but may lack business skills (marketing, accounting, computer). • Comingle personal and business funds in single account. • May rely on credit cards for expenses. • Limited ability to prepare good financials, complete tax reporting, provide projections with cost and profits. • Completely dependent on owner – no back-up resources.
Challenges
• Volatile cash flow, likely highly seasonal or periodic. Need for quick cash cycle products. • Limited time available is devoted to production which leaves little time for marketing, record keeping, planning, etc. • Limited infrastructure resources creating heavy reliance on seasonal crop/animal production. • Production hampered by the cost and requirements of certification for production, e.g. safe kitchen or organic. • Limited marketing ability – typically go to farmers' markets which are time and labor intensive.
Financing Needs
• Small loans ($5,000 - $10,000). • Use tied to production cycle of plants or animals; may need reduced payment during "off season"; likely to be multi-year due to limited excess cash flow and need to reinvest in farm for further growth. • Loans likely for additional crop/seed stock, fertilizer, growing materials, light infrastructure (fencing, mobile animal pens), light processing (i.e., freezer, mixing units, cooking/bake wear). • Loans will typically be 3-5 years.
Key Risk Factors
• Need for multiple sources of income so farmer is not solely dependent on farm income to live. • Farmer needs to have good understanding of what s/he is going to accomplish with funds, so funds are used appropriately and outcomes are identified and assessed. This will likely be a repeat borrower, so strong planning and coordination in the beginning can greatly improve outcome. • Limited fallback capacity if plan doesn't work. May be able to work with subsidy or guaranty program to minimize loan capital risk. • Need for good targeted TA (directly or indirectly). Farmer will have very limited time to meet so any training must be directly targeted to knowledge needed and presented in a format suitable for that person.
Analysis Ratios
• Global cash flow (personal and business). • Revenues & direct costs for primary business activities; cash flow analysis.

Small Full-Time Borrowers

General Characteristics
• Track record with one or several products; may be looking to expand product mix for longer season, or to expand on products through processing, retail and the like to increase profitability. • Likely need for capital investment at 100% borrowing. Borrowing may be for additional capital infrastructure or for working capital for new products. • Financials may be difficult to pull together in detail; historic results may not be indicative of future plans / use of funds. • Investment in new products does not have proven outcome; identifying/reaching new markets. • May have employees or be family business but likely very dependent on key person.
Challenges
• Cash flow may still be volatile but likely extends over longer season and potentially full year with good product mix and diversity. • Management of cash may be an issue. • May need cooperative or community resources (i.e. community kitchen, cooperative marketing and distribution, CSAs) to ensure cost effective sale of product. • Shift into more diversity may require more infrastructure which has no resale value (i.e., a barn, tubing for maple syrup, cold storage, retail store on-site). • Need for more sophisticated financial analysis – tracking of products, marketing program, competition, web site tracking. Need to identify, develop, expand appropriate sale outlets. • Approach business as a profession; with associated legal, employment, and insurance concerns.
Financing Needs
• Modest loans ($10,000 - $25,000). • Use may be tied to expanded production, additional activities (i.e. more animals, more types of crops, long term plant stock such as fruit or nut trees), year-round production, expanded capacity (i.e. tractor, greenhouse, barn), or improved retail (i.e. on-site retail outlet / farm stand, improved web site, labeling, marketing, storage, off-site processing). • Use may also be for multiple projects of varying durations and with different possible outcomes. Goal is to create more diversity so problem in one area is offset by success in another. • Loans will be multi-year (4-7 years), and may involve debt consolidation as farmer may have relied on friends, family and credit card.
Key Risk Factors
• Farm must be run as a business to anticipate and mitigate potential setbacks; record keeping which segregates product lines by revenues, direct costs, and allocated costs. Segregated business accounts. Proper tax schedules. Running as a tax shelter will limit future borrowing. • Need for wider business skills – organization, managerial, marketing, accounting - which may create new stresses on farmer. • TA is important here but must be close by, highly targeted and work with farmers' schedules. • Professional advisors and next level agricultural advisors can bridge to next steps in growth. • Tracking use of loan proceeds and having predefined outcomes to help farmer assess results and make real time adjustments for setbacks as well as new opportunities.
Analysis Ratios
• Farm/production cash flow. • Revenues & direct costs for all major existing business activities; cash flow analysis. • Projected revenues and direct costs for proposed activities. • Financial and cash flow modeling sufficient to assess financial risks.

Commercial Borrowers

General Characteristics

- Track record with mix of crops/products, some infrastructure, established marketing outlets.
- Need for capital investment at 80%-100% of borrowing.
- Adequate financial reporting but historic results may not forecast future results.
- Borrowing needs may be for expanded marketing tools – web site, bar coding, delivery vehicles, cooperative ventures.
- Demand for product(s) may outstrip capacity, creating working capital issues. May need to expand product line to keep or gain access to stronger commercial markets.
- Has employees and may be outsourcing some work. More complex model and owner will need to expand skills out of "production" and into management and oversight.

Challenges

- Reaching next level of scale requires working capital. Ability to properly price products and get product to the right outlet.
- If delivering product, route density analysis often missing. Management of larger delivery area.
- Bar coding for retail sales, with ingredient listing.
- Contracts to buy materials in bulk require careful cash flow management to fulfill payment terms.
- Employment increases – cost of hiring, labor issues, quality control, operations management.
- Liability insurance, legal status, accounting systems.
- Need for operations manager for scheduling, workflow, sales support.
- Access to larger and more predictable buyers (CSAs, Restaurants, institutional buyers, retail chains such as Whole Foods, wholesale buyers).
- Product processing to expand product mix and increase profitability requires R&D.

Financing Needs

- Medium size ($25,000-$500,000) to larger loans (over $500,000).
- Loans may be for specific purpose or project, such as building a production facility, creating a marketing clearing house, building a slaughter-house, and the like.
- Borrowers may be single farm enterprises or cooperative ventures.
- Financing enhancements may be available such as New Market Tax Credits, FSA, SBA, USDA, etc. There may be senior and junior debt levels and/or group of lenders.

Key Risk Factors

- Increased complexity of farm model and larger financial investment.
- Need for strong financial tracking and strong ability to understand and manage cash flow.
- Need for professional advisors from accounting, legal, insurance, to sales, marketing and computer/internet.
- Borrower may be overwhelmed by complexity of project/farm and could require support.
- May need help to bridge dialogue between senior lenders and farmer/owner.
- Larger overhead increases cash flow risk (less ability to downsize rapidly).

Analysis Ratios

- Farm/production cash flow.
- Fixed overhead.
- Capacity needs – i.e., equipment, storage, outbuildings, processing, land, long term crop production, multi-year production cycles, crop/animal rotation, and sustainability.
- Access to higher yield markets, value added processing.
- Operational costs of entering new markets, requirements of same.

Appedix II

CDFI Self-Assessment Tool: Small/Medium Scale Agriculture Sector Lending

I. Mission

Is an agricultural lending program in alignment with CDFI's core mission?	☐ Yes	☐ No
Has the CDFI designated the agriculture (ag) sector as a strategic priority?	☐ Yes	☐ No

II. Market Analysis – The Landscape

Is there demand from the market/sector to engage in agricultural lending?	☐ Yes	☐ No
Is there competition from other lenders/financial institutions in the sector?	☐ Yes	☐ No
Is there competition from other lenders/financial institutions for funding for the ag lending program?	☐ Yes	☐ No
What is the size of the borrower market?		
What is the risk profile of the average borrower?		
Does the CDFI have connections with TA, business development services (BDS) and other resources in the ag sector?	☐ Yes	☐ No
What is the political environment?*		

III. Capacity

Does the CDFI have internal resources to do market outreach and data collection to develop ag lending program?	☐ Yes	☐ No
Does the CDFI have internal operational capacity to manage an ag lending program?	☐ Yes	☐ No
Does the CDFI have internal lending staff resources to develop an ag lending program?	☐ Yes	☐ No
Does CDFI have agricultural underwriting/lending experience?	☐ Yes	☐ No
Is the CDFI willing to develop ag lending capacity--through training, hiring staff, etc?	☐ Yes	☐ No
Does the CDFI have a staff champion for the ag sector?	☐ Yes	☐ No
Does the CDFI currently have staff with industry knowledge of the ag sector?	☐ Yes	☐ No

Will the CDFI need to raise funds for ag lending program?	☐ Yes, to support lending staff	☐ Yes, to capitalize loan fund	☐ No

Would the CDFI consider developing an ag TA program in house?	☐ Yes	☐ No

IV. Financial Analysis

What is the risk tolerance of the CDFI in ag lending?	☐ High	☐ Medium	☐ Low

Does the CDFI have financial resources to develop an ag lending program?	☐ Yes	☐ No
Does the CDFI have internal loan capital for an ag lending program?	☐ Yes	☐ No
Does the CDFI have internal loan loss reserves for an ag lending program?	☐ Yes	☐ No

Potential sources of ag lending funds.	☐ Federal	☐ State	☐ Financial Institution	☐ Foundation/Donor	☐ Other

Annual projected interest income from ag lending activity?	☐ High	☐ Medium	☐ Low
What is the organizational risk?	☐ High	☐ Medium	☐ Low

Are their costs associated with source of ag lending funds?	☐ Yes	☐ No
Is the CDFI able/willing to do multiple deal structures in this sector (e.g. sub-debt, othe partnerships, direct, pari passu)?	☐ Yes	☐ No
Can the CDFI provide flexible repayment schedules based on borrower cash flow?	☐ Yes	☐ No

*"Political environment" refers to such things as pressure or support to enter the sector from the industry; of 'turf' issues around engagement with the sector from other organizations, lenders; or if the literal political environment (e.g., legislature, etc.) is positive or negative for sector involvement