More Options to Cash Flow Your Business

These days farmers have a lot more options when seeking alternative lending arrangements for farm business projects

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As land values and input costs continue to rise, alternative lending is becoming more common. Farmers are looking for more creative and flexible options to finance their business expansion, transition or diversification projects.

Country Guide explored some of the alternative financing options available with the proviso that there is no one-size-fits-all-solution, just as there is no one-size, cookie-cutter farm.

FAMILY AND FRIENDS

One of the oldest forms of alternative financing, still prevalent today, is borrowing from family, friends or others in your network. It can also be the riskiest if the same precautions aren't taken as when borrowing from a financial institution. That means agreeing in writing (preferably with a lawyer involved) on details such as interest rate, payment terms, term of the loan, and what happens if either party is unable to repay or passes away before the loan is repaid.

BRIDGE FINANCING

When a farm business needs short-term help to bridge the gap between their immediate financial needs and long-term goals, or to navigate through a period of transition or growth, short-term bridge financing may be the answer.

"Sometimes clients are coming to us because their financial institution has called in their loans. But it's also a young farmer coming in that has no established credit and they want to buy

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land and they need to establish their credit before a conventional lender will work with them," says Josée Lemoine, vice-president western Canada business development with Farm Lending Canada, a private lender since 2019. (They also own AgriRoots, an investment fund that specializes in alternative, short-term financing for farmers.) Since its inception, Farm Lending Canada has supported over 90 Canadian farm families, funding in excess of 90 agricultural mortgages, totalling over $125 million.

"For others, cash is getting tight because input costs went up and commodity prices aren't doing as well, and they're finding themselves with little cash, a mortgage payment coming up and a crop they need to put in the ground," she adds. "We can help them in these scenarios to get to the next phase."

Of course, there are any number of reasons that a business and a lender can reach the end of the line.

"In that scenario we might see buying them out, paying out whatever liabilities they have and then helping them transition to a new lender that is more aligned with where they're at," Lemoine says.

LEASING

Although not widespread, equipment or land leases have become more common in agriculture. Depending on the company, just about any type of agricultural equipment can be leased from tractors, combines and sprayers to grain bins, and grain and cattle-handling systems. It works especially well for farmers who prefer to update their equipment regularly. Leasing provides access to new or used equipment without a hefty upfront investment, leaving more cash inside the business operation.

Equipment lease payments are also generally less than loan payments used to purchase equipment outright, and leases are usually covered by warranties for repairs and maintenance that can save farmers time and money. There are significant tax benefits to leasing as well.

"Farmers are looking at alternatives that will give them better tax incentives or benefits, and that's where we are seeing a shift towards leasing of assets just because there are different write-off opportunities with that," says Saskatchewan farmer and accountant Lance Stockbrugger.

WHOLE LIFE INSURANCE

Borrowing against whole life insurance is another way to obtain business financing.

Whole life insurance is very different from term insurance, which is usually taken out for a specific length of time (10, 20 or 30 years) and does not result in a cash asset accumulating in the policy. Whole life insurance, by contrast, is more expensive to purchase but provides insurance coverage for your entire lifetime and builds a cash asset within the policy, called the cash surrender value (CSV). The policy owner can borrow against the CSV during the lifetime of the insured person.

It's common for a business owner to purchase whole life as part of a business transition plan. After a policyholder's death, it can help with estate equalization for family members who are not involved in the business, and with estate costs to help ensure a smooth business transition or wind-down.

"These types of loans can be very advantageous because they allow a business owner to obtain the long-term benefits of life insurance, while also freeing up cash to reinvest in their business in the short term," says Erin Smith, CEO of Alberta-based Grasslands Finance Corp, a financing company specialized in lending against whole life insurance that serves clients across the country (excluding Quebec).

People will borrow against their whole life policy at different stages of their lives and for various reasons (e.g., expansion, diversification, retirement), but inevitably it's when they start to think about a long-term plan that they call Grasslands Finance.

Grasslands doesn't sell insurance, but Smith emphasizes the importance of finding a good insurance broker to work with.

"It's important to find the right broker who is interested in working with you for the long term and has a good track record of servicing clients," she says. "These are long-term, expensive structures to enter into and you want to make sure you have a good partner who can guide you through it."

JOINT VENTURES

Although not common in agriculture, Stockbrugger says he is seeing more of these arrangements especially for situations involving higher value assets such as farmland or quota on a longer-term purchase.

"That could be looked at as a type of financing arrangement where people enter into a business arrangement where it might be tied to profits, so they are paid back based on profits," he says. "That's more of an investor-type arrangement, whether that's pension funds or individual investors or institutional investors. People want to have access to the industry but don't want to, or aren't capable of, doing the day-to-day operations."

VENDOR FINANCING

A similar arrangement to a joint venture is a scenario where a retiring farmer helps fund the transition of the farm to the next generation or perhaps a long-term employee or new farmer wanting to get into the industry.

"It's somebody who has lived the industry their whole life trying to give back, and they aren't doing it for free, they are benefiting from it, but also want to see this industry carry on," Stockbrugger says. "It can take any form, based on how creative and risk-tolerant or adverse you are in terms of how you want to structure it. Then it's just a matter of putting together the legal details to make sure both parties are protected. There are tax benefits for the vendor and it can assist the younger generation to get into farming."

ADVANCE PAYMENTS PROGRAM

It's true that farmers also have options available to them that others don't such as the Advance Payments Program (APP), a federal loan guarantee program that provides agricultural producers with easy access to low-cost cash advances. APP advances are available through 26 participating producer organizations across Canada.

Farmers can access a cash advance based on the value of the eligible agricultural products they will produce or have in storage. The federal government pays the interest on the first $250,000 of the advance. Farmers repay the advance as they sell their products. They have up to 18 months to fully repay the advance for most commodities and 24 months for cattle and bison.

The program helps improve farmers' cash flow and provides them with some marketing flexibility so they can sell their crops or livestock based on the best market conditions rather than a need for immediate cash.

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>
> **— ERIN SMITH**

BUSINESS RISK MANAGEMENT PROGRAMS

Although business risk management programs are not a form of financing in themselves, certain programs, such as AgriStability, AgriInsurance, AgriInvest and Livestock Price Insurance can be used to help secure financing with lenders and, in some cases, as security for the Advance Payments Program.

INCENTIVE PROGRAMS

Increasingly, lenders and other businesses and organizations are offering incentives for farmers based on their production practices that bring value beyond their own farm, for example environmental incentives for best management practices that result in reductions of greenhouse gas emissions.

An example is FCC's Sustainability Incentive Program that encourages the adoption of sustainable practices on farms. Developed with industry partners. such as the Canadian Roundtable for Sustainable Beef, Cargill, Dairy Farmers of Canada, Ducks Unlimited Canada and PepsiCo, Fertilizer Canada and McCain's, the program currently offers six programs covering different commodities. Programs offer a retroactive interest rate rebate for customers who achieve specific criteria defined by the industry.

THE EFFECT OF PROBLEM YEARS

Glengarry Farm Finance is a small investment fund, originally started by farmers, that offers short-term alternative lending options for farmers. It will only fund clients that it can steer back to a regular bank within its loan term, which is one to three years.

Most of Glengarry's investors are high net worth individuals. It has also formed a partnership with Farm Credit Canada who has committed $60 million to Glengarry to provide farmers with more flexible financing options when they need them the most. The deal was important to help Glengarry offer lending at lower rates than it had previously, and to make loans for larger amounts.

"We are looking for the loans where the bank has said 'We can't really get this done, please look elsewhere'," says Ric Luimes, Glengarry's credit manager and CRO. "Typically, that's a farmer that has had a couple of crop failures, although we are seeing cattle loans right now because the cattle industry had two back-to-back problem years in 2020 and 2021."

The cattle sector is a good example of how Glengarry can do things that a traditional bank can't. A big metric that banks look at before they decide on a loan is debt service coverage using a three- to five-year average.

"As a cattle producer trying to get money in 2024, and you didn't have your 2023 statements done yet, you would have had to use 2020, 2021 and 2022 as your average, and if you have two disasters in a three-year average you are not going to qualify at the bank," says Luimes. "We have the flexibility to say 2020 is not representative of normal, so we can take that year out and look at other years to get our average, and now the client doesn't look that bad. Even if the numbers are a little bit out, we can take that calculated risk because we have the flexibility to do so."

The biggest reason that most farmers struggle is related to cash flow. "The number one reason why loans get declined is insufficient cash flow to service the debt in probably 98 per cent of cases," Luimes says, adding it's a problem that is exacerbated by the high asset values in farming today. CG