Northwest FARM CREDIT SERVICES

BUSINESS TOOLS

Financing Agriculture: The Business Borrower-Lender Relationship

One of the most critical decisions a businessperson makes is choosing a lender. Because the agricultural industry depends on the sound use of credit to finance real estate, production assets and operating activities, a good relationship between a borrower and lender is important for long term business success. The borrower and lender have similar goals in that they want to ensure the long-term viability of their businesses. The borrower and lender should each have high expectations for the other in the relationship and be willing to discuss them freely. The purpose of this publication is to identify the important traits of a good lender and how you can be a valuable partner in the lending relationship.

What to look for when selecting a lender

Choose a lender that understands your industry and its people. Agriculture is a diverse industry, and each segment has its own unique needs. For a lender to make sound recommendations and develop the best financial package for you there must be common ground upon which to start.

Tip: Look for a lender that can provide financial benchmarks to help you evaluate your performance compared to others in your industry.

Look for a lender with the capacity to meet your borrowing needs

The lending institution should have the capacity to meet your current borrowing needs and future growth. Ask the lender about borrowing limitations in relation to individuals and industries.

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Look for a lender with competitive loan products and quality services

Search for a lender that provides loan products with competitive rates, and most importantly, flexible terms. Repayment schedules should mirror the timing of cash flows from the operation. A good lender will customize loans to fit your needs. Loan structure should be tailored to fit your unique needs and not restricted due to the lender's internal capital or term limitations. Select a lender that offers quality services in addition to their loan products. These may include cash management tools, insurance products, business planning services, educational opportunities, and others. These additional products and services complement loan products and can help save time and money by creating a total financial package for your business.

Tip: To thoroughly understand the financial condition of the borrower's business, three to five years of financial statements are preferred.

Choose a lender that has a stable staff with experienced employees

In a time of mergers and acquisitions, it's important to select a lender that can offer stability in a changing environment. Look for an institution that takes a team approach to servicing your account. This assures more than one person at the bank is familiar with your operation. There should always be someone on the staff acting as a backup in case the primary credit officer is unavailable or leaves the institution.

Get access to the decision maker

Choose a lender with decision makers that are accessible to you as a borrower. The person who analyzes the information on the loan application should be involved in making a decision on the loan. Also, the lender should share how loan requests are analyzed and decisions are made.

Choose a lender with a long-term presence in your industry

Your lender should support your industry during both prosperous and challenging times. The goals of your lender should include a permanent dedication to your industry and its people. Avoid lenders that begin lending to an industry while it's profitable, only to exit when times are tough. However, remember a good lender will not blindly say yes when it is more prudent to say no.

Your lender should have an up-to-date knowledge of credit and how it pertains to your industry

Look for a lender that can provide financial benchmarks to help you evaluate your performance compared to others in your industry. The credit officer should be willing and able to ask the tough questions and challenge your performance when it's below that of your industry peers. The lender should be a problem solver and facilitator. They should work with you to develop financial options and allow you to make the decision.

Select a lender that values business relationships more than just the transaction

Look for a lender that believes in the importance of developing a long-term relationship with you. You and your lender should grow together, benefiting from each other's success. The lender should be open to suggestions on what you would like changed or improved in the relationship. Notice if and how often the lender makes on-site visits to your business—this shows interest in your success and sincerity in the relationship. A good lender will follow up after the transaction and show appreciation for your business.

Find a lender that values trust, confidentiality and ethics

Discussions between you and your lender are confidential and should not leave the confines of the office. A good lender will not only earn your trust but will remain honest, even if it means telling you what you may not want to hear.

Tip: To request a current copy of your credit report, contact the local credit bureau in your area.

Look for a lender that can process your request in a timely manner

Crop and livestock production schedules require timely credit decisions to avoid adverse effects on cash flow and profits. Once the required information is identified and received, the lender should make a decision in a timely manner. Paperwork should be minimized to the extent possible.

Select a lender that communicates rates, terms, and conditions up front in a clear manner

Be aware of hidden fees, or the "Oh, by the way!" factors. There should be minimal surprises in the relationship. While the lowest interest rate may provide coffee shop bragging rights, it should be carefully considered in the context of the total credit package. You need to ask other questions that help you compare "apples to apples" and tell you the rest of the story. Is your loan being sold to the secondary market? Does your loan allow for prepayment? Does the loan require a balloon payment? Does your lender offer patronage?

Provide your lender with accurate financial information

A good borrower-lender relationship is built upon a joint understanding of the financial condition of the borrower's business. Three to five years of financial statements are preferred. These should include a balance sheet, cash flow statement and income statement. The cash flow projection should include "what if" factors concerning price, cost and capital acquisitions. The income statement may be the tax form, but an accrual adjusted income statement is preferred. As a borrower, you should have an understanding of your business' financial situation, even if an accountant or CPA is used to prepare financial statements. Additional information on personal debt, especially credit cards, should be provided. It's also important to provide documentation to support your financial statement entries. Lenders are generally required to verify information such as account balances. As your operation grows, you should be prepared to step up the quality of information presented. Audited or reviewed financial statements are often required when operations have revenues exceeding $10 million.

Provide a business plan

Your business plan should include a mission statement/strategic focus and both business and family goals. In today's volatile agricultural markets, your business plan needs to address specific plans for marketing your products.

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Tip: Choose a lender that has a significant stake in your industry. Their success should depend upon your success.

Your lender can better serve your needs if he or she knows your operation's current and future directions and how you plan to get there. A good business plan will look three to five years into the future and helps your lender understand where you are trying to take your business. Be prepared to provide information on the amount and stability of non-business revenue.

Maintain an honest and ethical relationship with your lender

Just as surprises by the lender are undesirable, the same is true for decisions made by the borrower. Inform your lender up front about significant business transactions, such as machinery purchases, purchase or sale of real estate, or changes in operating expenses. You should disclose all information that may be significant to the lender, such as insurance held, pending lawsuits and retirement plans.

Perform a personal consumer credit check on a regular basis

Most lenders use credit bureau reports to verify balance sheet information. Your use of credit will be considered by other lenders making credit decisions. Unfortunately, your credit history may contain errors or other items of which you are unaware. Periodically request a credit report to check for incorrect, unknown items or possible identity theft. Unless you contest any incorrect information, your requests for credit could be denied based on inaccurate information.

Maintain open and regular communication with your lender

A lender can be a valuable resource to assist with decisions and can help you avoid decision-making based upon emotion. Inform your lender of problems or changes in the business that may impact your ability to repay. Timely communication can minimize the impact of adverse situations and maximize available options. It's important that you allow the lender time to make a decision and this begins with good communication.

A successful relationship between a borrower and lender requires cooperation and professionalism by both parties. Like a chain, the relationship can only be as strong as its weakest link. If the preceding responsibilities are met, the borrower-lender relationship will prove beneficial for the lending institution and the customer.