

Financial Management in a Turbulent Economy

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Ag Profitability Conference

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Introduction to BS

- Farm background
- Grew up with little money (but we were not poor)
- Farm substituted labor for capital
- Minimized investments in depreciable assets
- Learned to cuss from my brother

Financial Management?

- Managing your money/wealth/investments/debt
- Often emphasize debt management—managing shortfalls in income—debt structure
- Also need to manage wealth—where to store it

Financial Management

- Your goals should dictate how you manage finances
- Possible goals
 - Wealth accumulation
 - Current income to spend
 - Debt reduction
 - Easier life
 - Retirement income
 - Reduce taxes
 - Donations to charities

Financial Management

- Need to recognize the implications of your goals
- There are tradeoffs
- Examples
 - Wealth accumulation—current income to spend
 - Current income to spend—debt reduction
 - Wealth accumulation—easier life

Financial Management

- Need to be aware of the environment in which you are operating
- Economy has been **TURBULENT**

U. S. Economy

- Sick!!!!
- Every button and lever and adjustment has been made to make it go, and it is still sputtering

U. S. Economy

- Extremely low interest rates
- Low saving rates recently that have now increased
- Consumer debt is high
- High unemployment
- Manufacturing base overseas
- About 1/4 home mortgages underwater

U. S. Economy

- Government debt is high
- Value of the dollar has been dropping
- Stock market crashed –low on March 9
- Stock market has rebounded a great deal, but still highly volatile
- Trade deficit is still large
- Credit standards have increased
- Large number of banks have failed

Economy—Agriculture Ties

- Value of the dollar
- Interest rates
- Credit Availability
- Credit Standards
- Inflation
- Energy prices

Economy—Agriculture Ties

- Demand for land from Off-farm investors
- Alternative investment returns (stock vs. land)
- Off-farm income for producers

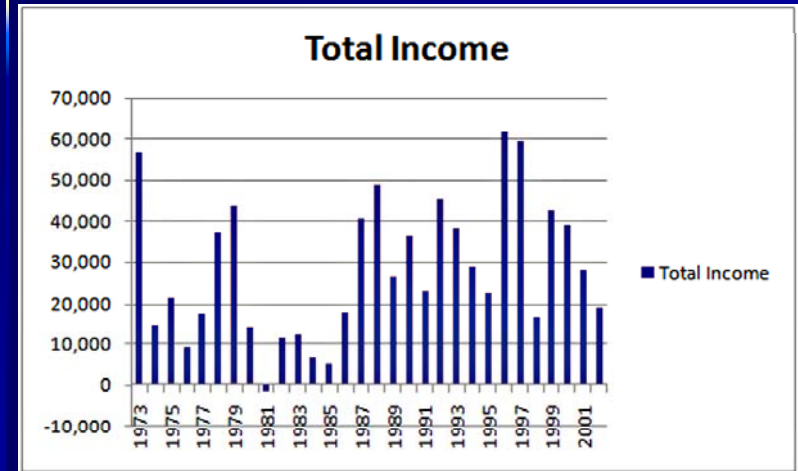
Issues to address

- Farm Income
 - Will it last?
- Options for Storing Wealth
 - Reinvest in Production Ag
 - Invest Outside Ag

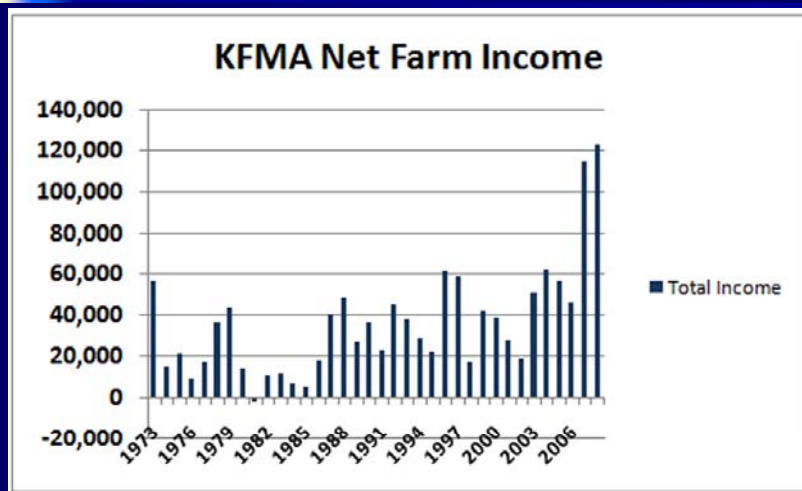
Farm Incomes

- "Economic profits" do not last long in a competitive market

KFMA Net Farm Income



KFMA Net Farm Income



Farm Incomes

- Recent good years for some
 - Great range in income
 - \$281,800 for high 25%
 - -\$26,147 for low 25%
- Big Issue---Will this last?

Farm Incomes

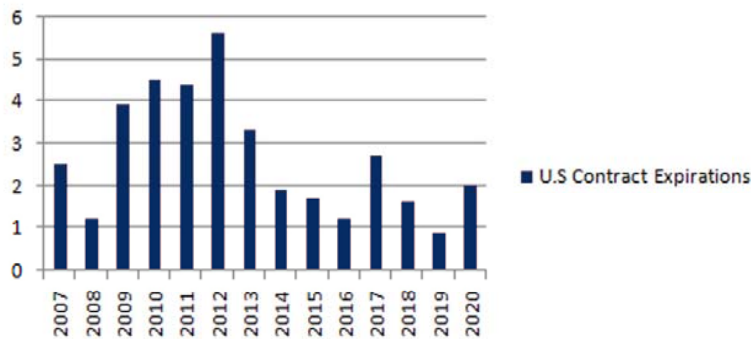
- Does the world have enough extra capacity to destroy economic profits?
- We are not at Equilibrium
 - Crops
 - Livestock

Farm Incomes

- Does the world have enough extra capacity to destroy economic profits?
- Ethanol
 - Using about 1/3 of US corn production
- CRP
 - 34 million acres in program at present

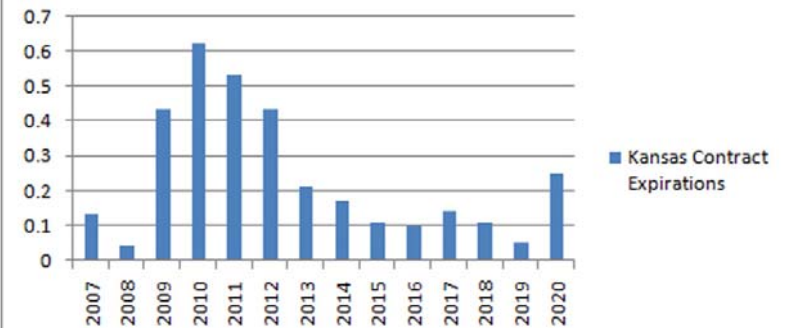
CRP Program

U.S Contract Expirations in Million Acres



Kansas CRP Program

Kansas Contract Expirations in Million Acres



Farm Incomes

- “Economic profits” do not last long in a competitive market—What about this time????????????????

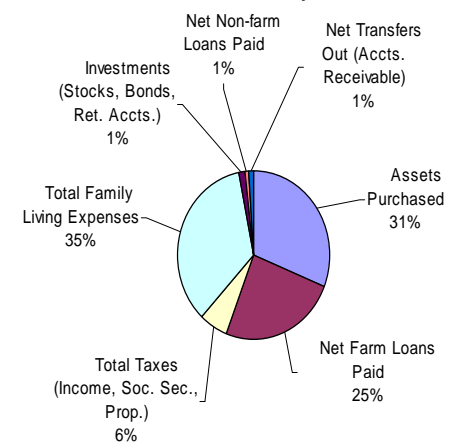
Storing Wealth

- Where should wealth be stored?
 - Botswana--cattle
 - My farm experiences—hay in barn and supplies

Storing Wealth

- Reinvest everything in Agriculture?
- Diversify outside of agriculture?

Chart 5. 2002 Discretionary Uses of Funds

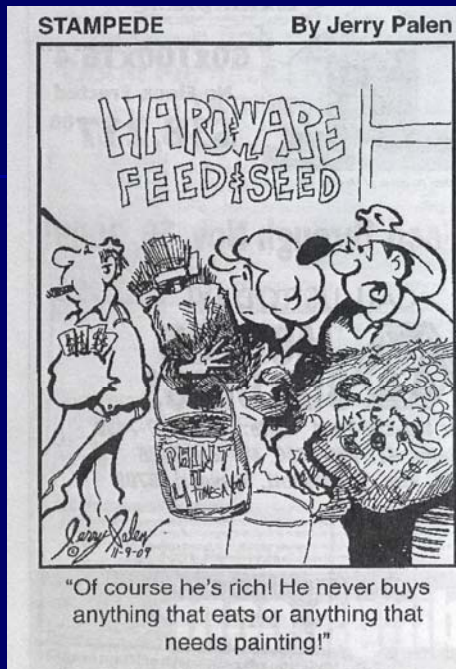


Reasons to Reinvest in Production Agriculture

- Growth and survival—economies of scale
- Growth for future generations
- Improved quality of life (new machinery)
- Great rate of return
 - For some
 - Not for everyone
 - Should be adjusted to after tax and adjusted for risk
- Familiarity (important in risk evaluation)

Storing Wealth

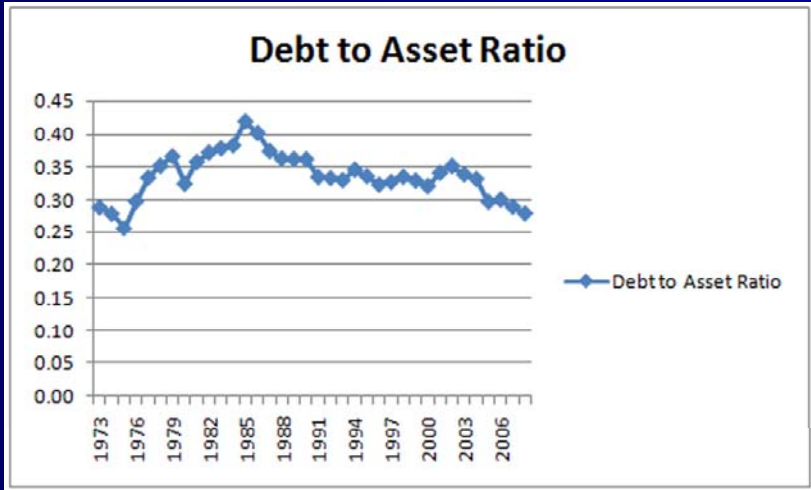
- Where should wealth be stored?
 - Grain in storage since do not need the cash
 - Machinery
 - Pay down debt
 - Land



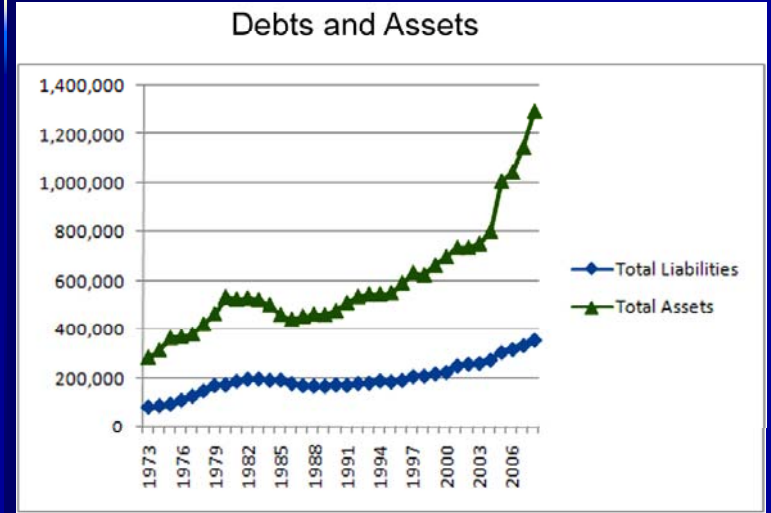
Storing Wealth

- Pay down debt
- Generates “credit reserves”

Debt Levels



Total Assets and Total Liabilities



Store Wealth

- Buy more land

Land values

- Land Value per Acre =

Income per Acre

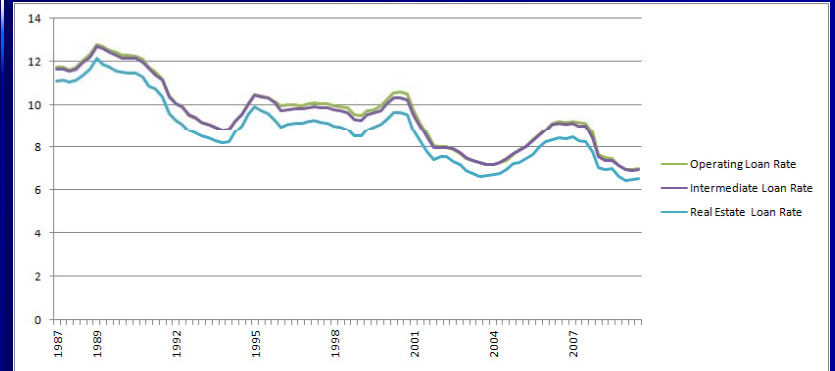
Interest Rate

Land Values

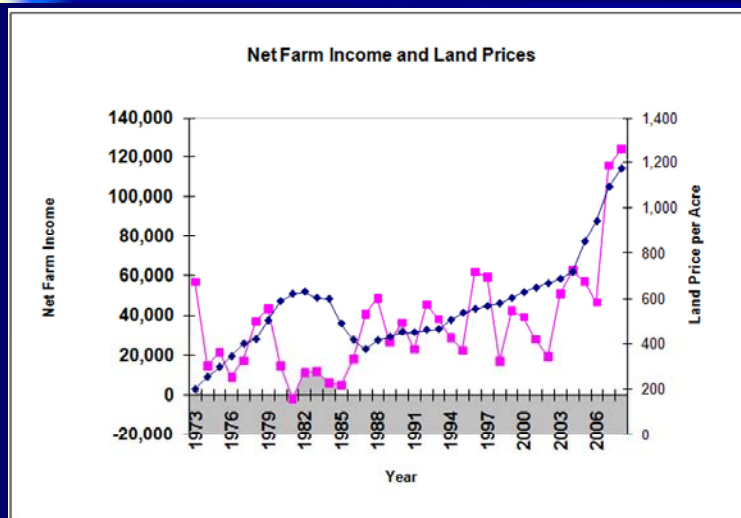
- Income goes up, land value goes up
- Rates go up, land value goes down

Interest Rates in Kansas

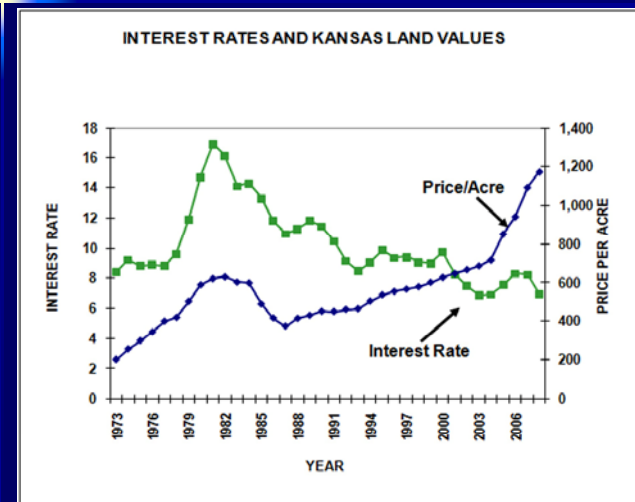
Kansas City Federal Reserve Data



KFMA Net Farm Income



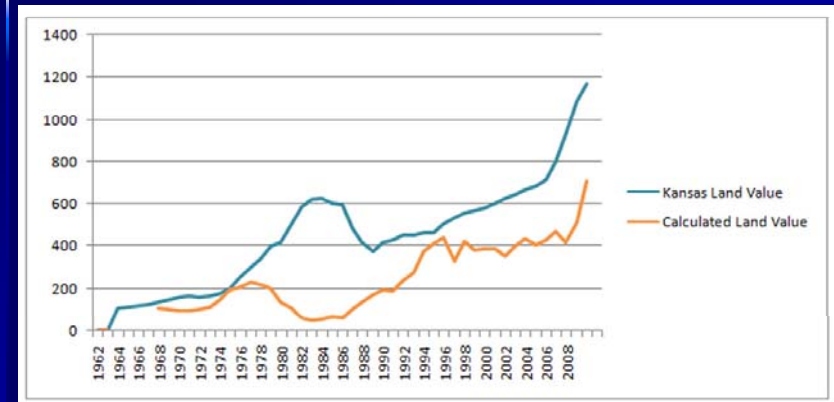
Interest Rates



Impact of History

- Markets can do whatever they want
- BUT, the farther they get from the fundamentals, the greater the risk of a correction

Actual and Calculated Land Values



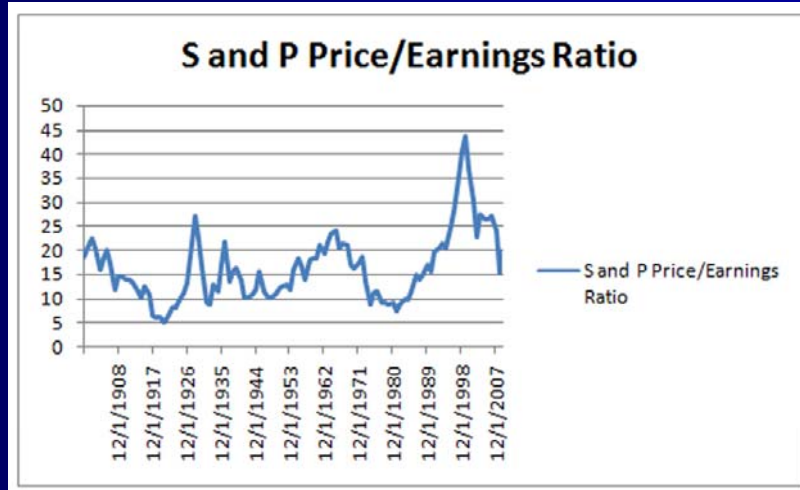
Asset Bubbles

- Big concern in economics
- Have had many recently
- Why do bubbles develop?
 - Feedback loops
 - Greater fool theory

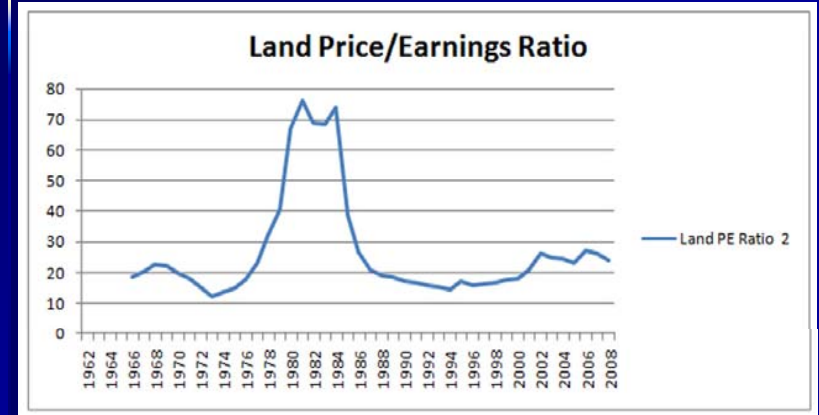
What we learn from the stock market

- PE Ratio= Price per share/ Earnings per share

Standard and Poors Index



Land P/E ratio



Storing Wealth

- Where should wealth be stored?
 - Grain in storage since do not need the cash
 - Machinery
 - Pay down debt
 - Land
- Invest off the farm

Reasons to Invest outside Agriculture

- Rates of return in the stock market have in some periods been substantially higher than returns in agriculture
- Diversification
- No good expansion possibilities
- Need to add a lumpy input
- Stage of life of the operator
- No children interested in farming

Investing off the Farm

- General order of preference
 - Options that receive a matching contribution
 - Options with tax advantages
 - Roth IRA
 - Traditional IRA
 - Options with no tax advantage

Roth IRA

- Tax Free earnings
- Contributions are nondeductible
- Modified adjusted gross income must fall within limits given by IRS
- \$5,000 for 2009 (\$6,000 if over 50)
- Some flexibility in withdrawals

Traditional IRA

- Tax-deferred earnings
- Contributions are deductible if you do not have an employer sponsored plan
- Must be under 70½
- \$5,000 for 2009 (\$6,000 if over 50)
- Withdraw after age 59½

Storing Wealth

- Check your goals
- Diversify
- Return “of” capital vs. “on” capital
- Have to take risk to get return