WISCONSIN DAIRY TASK FORCE 2.0
SUB-COMMITTEE ON ACCESS TO CAPITAL
MINUTES

October 15, 2018

The Sub-Committee on Access to Capital of the Wisconsin Dairy Task Force 2.0 met on Monday, October 15th, 2018 beginning at 10:00 a.m. at the Offices of the Wisconsin State Patrol, located at 23928 Lester McMullen Drive, Tomah, WI 54660-5376 in the Downstairs Conference Room.

Call to Order

Sub-Committee Chair Brad Guse called the meeting to order at approximately 10:00 a.m.

Members Present

Brad Guse, Don Hamm, John Accola, Paul Scharfman, and Darin Von Ruden.

Ex officio member Representative Don Vruwink was also present. Mark Stephenson, Neil Kline, and Kevin Burnhardt were also present.

Minutes

Welcome and Introductions

Members of the Sub-Committee introduced themselves.

Kevin Burnhardt, Professor of Agribusiness at the University of Wisconsin-Platteville and with the Center for Dairy Profitability at the University of Wisconsin-Madison, served as the Sub-Committee’s resource person.

Chair Guse emphasized the importance of frankly stating opinions and being honest with each other. He reviewed the tasks before the Sub-Committee, which are:

1. Review issues identified by the full Task Force and refine those issues into as many carefully worded, separate issues as necessary (a sentence or paragraph for each issue, not just a bullet point).
2. Consider the working name of the committee.
3. Consider possible solutions to each of the issues identified by working with your resource person.
4. Classify each proposed solution into one of the following spheres:
    a. Individual business
    b. State or regional organization
    c. State policy or dollars
    d. Federal policy or dollars

Task Force Chair Stephenson identified the central challenge of access to capital for both farmers, processors, and auxiliary services.

John Accola noted the difference in financing needs between large and small farming operations, and the difficulty that stems from those differences as a result. Chair Guse agreed, and extended the challenge to the diversity of plant size.

Chair Guse then asked the group where a farmer who wants to expand to a 3,000 to 5,000 cow dairy would be able to secure financing for such a venture. Who would take on a loan of that size by themselves?

Mr. Accola noted that BMO has taken on loans of that size recently. He also noted that perhaps dairy has a unique challenge when it comes to securing financing because of the unpredictability of the industry.

Referencing the average debt-per-cow ratio, Chair Guse asked how that would limit the ability of a small, community bank to finance such an expansion, suggesting that the increasingly large financing needs of expansions are putting such projects outside the capabilities of smaller lending institutions. The result is a decrease in access to capital in rural settings by limiting the players in a lending market or requiring participators, which works fine in a strong economy but does not work as well in a slower economy. Chair Guse noted a recent expansion example he saw where a local bank determined they would need 16 other banks to participate in the loan in order to finance the project.

Paul Scharfman suggested that part of the Sub-Committee's task was to chart a course for the growth of dairy processors and other manufacturing companies in rural Wisconsin. He pointed out that financing building in rural areas is more difficult than financing building in more densely populated areas. This culminated in the idea of public credit enhancements, where the government guarantees loans to manufacturers in rural areas whose growth has outstripped their asset base. Mr. Scharfman tied this idea to a larger issue, which he felt was that there are significant "holes" in the financing of rural enterprises.

Mr. Scharfman explained that it is difficult in light, rural manufacturing (in his case cheese production) to obtain capital because the building, which is a highly-specialized, single-purpose structure relatively isolated from large population centers, is of little collateral value to a bank should the enterprise fail. If the same building were built near a large population center, it would have a higher collateral value because it could be more easily repurposed.

Mr. Scharfman said that a potential solution to this issue is to propose the creation of a state program that would guarantee loans for business in this situation, and in similar situations throughout the dairy industry.

Mr. Accola noted the connection to the land dairy farmers have, and the importance of securing long-term profitable margins for dairy farmers.

Mr. Scharfman articulated the view that there seems to be two Sub-Committees here. One is focused on best-practices education, which Mr. Scharfman feels is not part of the mission of the

Access to Capital Sub-Committee. The Access to Capital Sub-Committee, according to Mr. Scharfman, has the mission of charting a path to capital which combines educating borrowers on their options, clearly delineating the requirements for obtaining that capital and impressing upon borrowers the responsibilities inherent in that capital's reception.

Darin Von Ruden noted that many dairy farmers do not want to give up control, and that the issue of education, while there are other sub-committees who will be dealing with it, needs to be discussed in the Access to Capital Sub-Committee. He also articulated the importance of diversity, and his concern that capital is increasingly being concentrated in fewer and fewer hands rather than expanding the number of people with capital. Consolidation in the banking industry is a concern for him as well. He also noted the challenge of limited processing capacity in the context of dairy expansion projects and agreed on the need for the Sub-Committee to create a clear plan moving forward to address capital access issues.

Mr. Von Ruden then asked Chair Guse, in his capacity as a banker, what the asset value of many of his customers looks like. Chair Guse noted that the special use building dynamic articulated by Mr. Scharfman applies to dairy infrastructure on farms as well. The collateral values of those buildings is very low, and the sale of a 50 cow dairy operation will yield very little, as would the sale of a 300 cow dairy operation. To gain a meaningful collateral value, the site needs to be capable of receiving CAFO permits and be large enough to handle 6,000 cows.

Mr. Scharfman felt confident that this significant barrier (the low collateral value of rural, special use buildings) could be addressed legislatively via a loan guarantee program.

Chair Guse noted that the state already does something like this with other loan guarantee programs. He also noted the scale of these guarantee programs has not kept pace with the increasing scale of financing needs, and that the challenge of these programs is the cost of administration and loan servicing.

The group then worked to identify holes in the dairy lending landscape. In addition to holes in rural, small light business loans and loan size, the group created the following chart to identify holes in access to capital:

	Dairy Farm	Processor	Support and Infrastructure	Dairy Supply
Capital Expenditures	Funding for beginning/transitions and Larger Expenditures			X
Building and Fixtures	X/O	O	X/O	X/O
Equipment	X	X	X	X
Working Capital	X/O	X	X	X/O
Ongoing	X	X	X	X
Start-up/New	O	O	O	O
Environmental Technology	O	O		O

Following this discussion, the group moved to focus on outstanding issues, particularly financial literacy, which they determined was a barrier to capital access.

Chair Guse noted that it is quite usual in his role as a banker to refer potential borrowers to consultants to help create business plans, and he noted that the number of farmers who use financial records to make decisions is quite low. He said that the bulk of farmers use records for taxes and production information, not decision making.

Mr. Burnhardt felt that financial literacy is a barrier to capital access because it is a prerequisite to meaningful and serious conversations about financial options with lenders. He also articulated the view that market access for cheese makers, and the resulting barrier to entry for new cheese makers, is related to the issue of access to capital because the increased prevalence of cheese makers in rural areas increases the collateral value of all of their plants while also increasing the demand for milk, and impacting milk prices for farmers. Chair Guse noted that the Markets Sub-Committee is well positioned to work on market access issues.

Chair Guse noted that another precursor issue for access to credit are risk management tools, and asked whether or not the current battery of tools are best suited for not only farmers but processors as well.

Lunch

Lunch occurred at 12:15 p.m., and the Sub-Committee reconvened at approximately 12:55 p.m.

Chair Guse noted that Representative VanderMeer stopped in during the morning session.

The Sub-Committee began work on making a specific list of challenges developed from the table above. The list of challenges is below:

1. Rural special purpose structure financing collateral valuation constraints
    a. Special purpose-not easily transferred to new ownership.
        i. Physical, locational, and structural obsolescence.
    b. Less collateral value
    c. More cash down
2. Cycle bridging funding
3. Start-up and transition financing
    a. Financial literacy
    b. Mentorships
4. Environmental compliance emerging technology financing
5. Willing players in the agricultural lending marketplace?

Prior to the discussion on Cycle Bridging Funding, Don Hamm noted that in his view, there is capital available from unconventional lenders if the business has cash flows and a business plan.

The Sub-Committee decided to meet on January 23rd, 2019.

Adjournment

The Sub-Committee adjourned at approximately 3:00 p.m.

Minutes drafted by Neil Kline.

Minutes approved by sub-committee during November 16th, 2018 Teleconference.