

AGRICULTURE

Raising Capital in Agriculture

Top 5 Things You Should Know

Raising capital in today's financial landscape is not without its challenges for today's farmers and producers. The current Canadian landscape suggests that investors believe there is more capital than good investment opportunities. With the expectation of low interest rates and a weak Canadian dollar, there are positive signs that suggest increased opportunity to source and raise capital for business in Canada.

1. Innovation is power

Business owners have made investing in innovation a priority. Agriculture producers have been among the most active, investing in advanced machinery and equipment providing faster processing times. Understanding the need for assistance, various governmental agencies have earmarked substantial dollars to aid growers in making innovative investments in their operations including non-repayable grants and non-interest loans. Most of these loans are structured with deferred repayment terms for one year and designed to assist with managing cash flow. In today's financial landscape, businesses who are able to tap into this kind of financing have a significant advantage.



2. Security—buyer beware

The forms of security sought after by lenders are fairly common in the current marketplace. These typically include corporate and personal guarantees and general security agreements over some or all assets of the business. However, the inclusion or exclusion of the personal guarantee requirement, and the dollar value of the guarantee, are often areas of review. A careful review by a lawyer and accountant is a worthwhile practice before signing off. Often times, security clauses can be altered or removed all together through negotiation.

3. Shop around

Whether looking to expand, refinance or acquire a business, businesses typically look for financing from their existing lender or bank. The commercial lending marketplace is extremely competitive and lenders are constantly looking for good investments to place their capital. A customer is well served to seek the best deal from three or four lenders. The benefit is three-fold: 1) Going to multiple lenders ensures the best rate as healthy competition typically results in a better bargaining position. 2) Competition promotes greater urgency and a faster close of the transaction. 3) Some lenders are willing to invest more than others.

4. Think outside-the-box

Many entrepreneurs have tapped into new and interesting ways to raise capital for start-ups, expansion and various projects. Ventures such as crowdfunding are currently being used to help raise capital for farm start-ups and expansions. The concept of crowdfunding involves the funding of a goal or project through leveraging of small contributions from many people. It is widely used in support of charitable causes and disaster relief, however it also lends itself well to business uses. Whether the funding provides an investor reward (financial or non-financial) or donative, the possibilities are endless in attracting investors.

5. Eyes wide open

There are a number of factors and pitfalls that should be considered before starting to invest and commit dollars into a new project or business venture. 1) Applying for a loan costs money – many do not know that the banks charge a fee to process a loan which can run from a few hundred to a few thousand dollars depending on the size of the loan. Some lenders have an upfront, non-refundable fee which means even if obtaining the loan is unsuccessful, the fee is still owed. 2) Most lenders require a significant amount of due diligence be performed prior to loan approval. This typically involves having a set of pro-forma financial projections prepared, producing appraisals, providing personal net worth statements, etc. All of this requires upfront investment from the borrowers before the loan is processed. 3) Very few loans are actually approved locally. Most banks send loans to their credit department that makes the final decision. This process typically involves requests for additional information or further work be done before the loan is approved. Generally, such tiered structure results in longer processing times for loans on average and business owners have to be prepared to wait it out. 4) Lenders have a number of different metrics they use to assess credit risk and which businesses make good candidates for a loan. The most important criteria used by lenders is the value of the underlying assets and how much cash flow the business generates or EBITDA (Earnings before Interest, Taxes, Depreciation and Amortization). Lenders have the ability to loan up to a percentage of the assets they are funding; however, they also evaluate the level of EBITDA generated by the business to determine if the business can service the debt. In some cases, lenders are looking for a debt service ratio of at least 1.25 to 1. Meaning that for every dollar of debt repayment required, the business must generate \$1.25 of cash profit. 5) Other benchmarks exist on an industry by industry basis which may be unknown to many. For example, currently some commercial lenders are operating with restrictive guidelines when it comes to lending to dairy farms. Producers that are leveraged above the lenders' benchmark are at high risk for meeting their debt service obligations in the view of lender. As a result, anyone looking to purchase an existing dairy farm will require a significant amount of equity in order to meet the demands of the bank to partner on the deal.

How BDO can help

BDO helps clients operating in the agriculture sector navigate the challenges of today's marketplace and zero-in on the opportunities within the financial capital landscape. To learn more about how BDO can help, please contact Gerry Lanigan.

To learn more, contact your local BDO office or:



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About BDO

One of the nation's leading accounting firms, BDO Canada provides assurance, accounting, tax, and advisory services. As a member of the BDO international network, which spans more than 150 countries and 1,400 offices, BDO provides seamless and consistent cross-border services to clients with international needs.

About BDO's Agriculture Practice

BDO's dedicated team of professionals works with producers, agribusiness owners, farm organizations, and co-operatives, offering a full range of assurance, tax, business transition, and other services to help them succeed. As farms evolve and leverage new methods to streamline their operations, cut costs, and increase production, our professionals are ready to advise on how to maximize these investments for success.