Schools of Banking

Agricultural Lending School

Session Objectives

MEGA FORCES IN AGRICULTURE AND AGRILENDING – SESSION OBJECTIVES

- Describe trends that are influencing the agricultural industry.
- Have a better understanding of agriculture's strategic position.
- Comprehend structural changes in agriculture and rural communities.
- Understand trends in the agrilending community.
- Illustrate the importance of the general and global economy to the agricultural economy.

AGRICULTURAL FINANCIAL STATEMENTS SESSION OVERVIEW & OBJECTIVES

OVERVIEW

Financial statements provide the basis for sound financial and credit analysis, as well as the information needed for decision-making. These statements, when properly prepared and interpreted, enable the lender to effectively evaluate credit requests. The financial statements needed include:

- Balance sheet
- Income statement
- Statement of owner equity
- Cash flow projection
- Statement of cash flows

Recognizing the interrelationships among these financial statements benefits both the borrower and the lender. When integrated, the information contained in the statements will link past and present performance to projections of future performance. This requires careful coordination on the part of the preparer of the statements.

The various financial statements can follow many different formats. It does not matter which format is used as long as the statements are complete, accurate, and provide all essential information. This discussion will focus on the concepts underlying the preparation and analysis of financial statements.

AGRICULTURAL FINANCIAL STATEMENTS – OBJECTIVES

- Identify characteristics borrowers desire in a lender and characteristics lenders desire in a borrower.
- Identify the five financial statements needed to report financial information for an agricultural business, and the interrelationships among those statements.
- Complete a balance sheet in accordance with the recommendations of the FFSC.
- Calculate deferred taxes for an agricultural business.
- Prepare an accrual-adjusted income statement, using the information reported on a Schedule F tax return and beginning and end-of-year balance sheets.
- Understand the organization of a statement of owner equity and how to use it to explain changes in owner equity.
- Complete a cash flow statement and a statement of cash flows and understand how to use each statement to analyze the liquidity of an agricultural business.

AGRICULTURAL CREDIT ANALYSIS & DECISION MAKING – SESSION OBJECTIVES

- Become acquainted with the key information and variables needed in credit analysis
- Understand how to calculate ratios and other guidelines used to analyze the financial performance of a business
- Differentiate credit analysis techniques, depending on size and complexity of loan size
- Become familiar with a systematic approach to analyzing the use of agricultural credit using ratio and non-ratio indicators
- Be aware of measures that indicate strong and weak financial performance and communicate them on a professional basis
- Become familiar with the various financial strategies that can be implemented to ensure financial success
- Develop a better understanding of how personal and business characteristics and the business environment can influence credit success.

CREDIT SCORING & RISK RATING SYSTEMS FOR AGRICULTURAL BANKS – SESSION OVERVIEW & OBJECTIVES

"A Risk Rating System Designed to Enhance Credit Analysis, Not Replace the Loan Personnel"

OVERVIEW

A major result of the financial crisis in agriculture during the 1980s was increased lender awareness of the importance of credit assessment methods and analysis. Changes in the structure of agriculture, deregulation of banking, increased oversight by regulators, increased competition, and expanded lines of products and services have put substantial pressure on agricultural banks to increase efficiency and minimize risk. This equates to profits. The agricultural lending field is moving toward more standardization of analysis. This, along with time pressures on the lending staff and the lending function, has placed a premium on time management in the lending process for the 1990s and beyond.

These changes have increased the importance of methods and techniques, which accurately measure potential risk and profits of a particular loan in a time efficient manner.

OBJECTIVES

- Discuss potential benefits and pitfalls of a risk rating or credit scoring system.
- Present an overview of which variables agricultural banks are using to measure credit quality.
- To discuss how a system is weighted, developed, and validated.
- To provide guidance in the implementation of a system into a bank's operation.
- Illustrate a credit risk rating system and how it can be used in pricing a loan.

PROBLEM LOANS – SESSION OBJECTIVES

- List the major causes of problem loans.
- Identify the early warning signs of problem loans.
- Identify alternative solutions to dealing with problem loans.
- Explain the liquidation alternatives available for dealing with problem loans.
- Recognize the advantages and disadvantages of debt restructuring for problem loans.
- Understand the differences among Chapters 7, 11, 12 and 13 bankruptcy proceedings.

- Apply proper corrective actions to problem loan situations.

- Define the negotiation process and identify key elements of a successful negotiation

- Recognize the importance of establishing a negotiating position, maintaining control, and closing a negotiation.

STRUCTURING AGRICULTURAL LOANS – SESSION OVERVIEW AND OBJECTIVES

One of the most powerful tools at a loan officer's disposal is loan structuring. Loan structuring for new loan applications entails matching the terms of a loan package to the purpose of the loan in a way that serves the interests of the borrower and the lending institution. Loan structuring can also be used to improve the financial status of existing marginal loans. Proper loan structure may improve the repayment ability and liquidity of the borrower; thus, decreasing the risk to the lending institution. Conversely, a poorly structured loan may adversely affect repayment ability and long-term profitability of the borrower, thereby increasing the lender's risk exposure.

The key determinants of loan structure for new applications are the borrower's repayment capacity, loan purpose and loan security. The borrowers projected earnings will dictate the amount of structured payments the operation can afford. The loan package should match the maturity of debt to the useful life of the asset (short-, intermediate-, and long-term). A lender must also meet collateral guidelines and other underwriting standards of the lending institution. The two main tools for loan structuring are repayment plans and loan conditions or covenants. A loan officer should use these tools to construct a loan package that benefits the borrower and the lender.

SESSION OBJECTIVES

Following the successful completion of this session, you will be able to:

- Identify the key elements of loan structure.

- Recognize the different structuring tools available today.

- Explain different repayment terms and identify how repayment terms affect the risk of loan default.

- Explain the differences between revolving and non-revolving lines of credit.

- Recognize the differences between structuring short-term, intermediate- or long-term credit.

MARKETING – SESSION OBJECTIVES

- Calculate the breakeven price for each commodity produced.
- Determine how to achieve the breakeven price through the use of marketing strategies.
- Develop a basic working knowledge of marketing terms and commodity pricing strategies.
- Determine which marketing strategies are the most appropriate in order to achieve the highest net profit and to limit exposure in a volatile market, ultimately reducing commodity price risk and maximizing overall profitability for the customer and the bank.