

FARM BUSINESS FACT SHEET

FARM BUSINESS MODELS

Farm business models – why consider a change?

PHOTO: NICOLE BAXTER



Key points

- Corporate farming businesses manage overhead costs, financial risk and increase their access to capital investment by operating with a clear separation of farm asset ownership and business management and a reliance on employed labour.
- Using this corporate approach to develop a tailored, alternative farm business model has the potential to produce a more profitable and resilient family farm.
- Alternative farm business models can enhance profitability, provide more effective risk management (by sharing the risk with others) and assist with business succession.

Peter and Toni Unger, Alectown, New South Wales.

BUSINESS MODEL VS STRUCTURE?

A farm business model is commonly mistaken to mean 'business structure', or the combination of legal entities for business operation and asset ownership, such as a partnership, trust or company.

While legal entities are important, they are only part of the puzzle and may not take into consideration the foundations for a successful farm business. The business entity is best addressed in the later stages of setting up or restructuring a farm business model, matching the entity to the needs of the business and people.

AN ALTERNATIVE APPROACH

The family farm business model, where the land is owned and operated by the family, has generally served Australian agriculture well.

In this traditional family farm model, farm assets and farming operations, including management and labour, are usually provided entirely by the family. The contribution each resource makes to the farm business is typically not formally valued.

However, there are situations where the internal contribution of the farm's assets and operations will not

TABLE 1 Typical ownership and access arrangements for farm resources within business model 'types'.

Farm resources	Farm family	Leasing	Share farming	Contracting	Joint ventures
Land ownership	50 to 100% internal	100% external	100% external	100% internal or external	100% internal or external
Irrigation water ownership	50 to 100% internal	100% internal or external	100% internal or external	100% internal or external	100% internal or external
Livestock ownership	100% internal	100% internal	100% internal or external or shared	100% internal or external	100% internal or external
Management access	100% internal	80 to 100% internal	80 to 100% internal	100% internal	100% internal or external
Labour and machinery access	75 to 100% internal	80 to 100% internal	80 to 100% internal	25 to 100% internal	100% internal or external
Working capital access	100% internal	10 to 30% internal	10 to 30% internal	10 to 30% internal	100% internal

Note: 'internal' is owned or supplied by the farm business operator, 'external' by another party.

always deliver the best outcome for the business or the people involved.

In alternative farm business models, farm assets and farming operations are separated, allowing some to be provided by the business owners/operators and some by other parties, with each being rewarded for their respective contributions.

This fact sheet discusses some of the issues to consider when determining if an alternative farm business model could deliver benefits for your farm business.

THE EVOLUTION OF ALTERNATIVE FARM BUSINESS MODELS

Corporate farming is based on the separation of farm business resources, with a clear delineation of farm asset ownership and business management and reliance on employed labour for farming operations¹.

Within this model, farm assets and operations are commonly separated in the business structure to protect assets from operational risks by breaking down the farm business into distinct business resources.

An increasing number of family farms are evolving towards this corporate model by changing the mix of business resources. Sometimes

referred to as 'family corporates', many of these enterprises operate with formal board and administrative structures, as well as employed staff².

BENEFITS

Modifying the family farm model, or developing an alternative model to include some external contribution of assets and/or operations, can deliver greater flexibility and rewards. It may be as simple as 'tweaking' the traditional family farm model to include contracting, through to developing more complex models such as joint ventures or equity partnerships.

Alternative farm business models can assist growers or 'farm business operators' to achieve:

- **enhanced profitability** by improving cost structures and access to resources;
- **more effective risk management** through sharing risk with other parties;
- **business succession**; and
- **increased access to capital** for growth and operation, reducing the reliance on debt funding.

While adopting an appropriate farm business model can help address these 'drivers', business success also depends on the ability to manage and operate the business well.

A MIXED BAG OF FARM BUSINESS MODELS

Due to the range of personal and business needs combined with differing requirements for resources, most farms operate using a mix of business models. For example, family farms now typically operate with some leasing, some share farming and/or some contracting.

The level of asset ownership and contribution to farming operations within each model varies significantly depending on the business circumstances.

These variations mean it is not possible to define discrete business models; rather it is more appropriate to consider model 'types'. Common farm business model 'types' include:

- family farming;
- leasing land;
- share farming;
- contracting (including machinery, labour and/or management); and
- joint ventures.

Within the model types, the ownership and access arrangements for farm resources can range from completely 'internal' (business owners/operators) to completely 'external' (other parties), as described in Table 1.

Farm business management is based on decision-making, choosing a path for your business that has acceptable reward, both financial and non-financial, for acceptable effort with an acceptable level of risk³. What is 'acceptable' will vary from business to business and person to person. It is essential that farm decision-making includes all key people in the farm business.



PHOTOS: NICOLE BAXTER

Anna-Lisa Newman farms with her husband Craig near Varley and Lake King in Western Australia.

IN FOCUS

BASIC PRINCIPLES OF THE FARM BUSINESS MODEL

The following principles are critical to the success of farm business models:

- The farm business can be broken down into business **resources** (assets and operations);
- The resources help define the relative **contributions of different parties** to the farm business; and
- The contributions of each party to the farm business can be **valued and rewarded**.

Land is the most common example of a resource that is valued and rewarded. Lease payments made under lease agreements are a 'reward' for the contribution to a farm business.

WHICH FARM BUSINESS MODEL?

Alternative farm business models cannot be selected 'off the shelf' and implemented. They need to be developed to suit personal and business needs, focusing on people, finances and resources.

When considering the suitability of alternative farm business models for your business, it is essential to understand:

- what are the drivers for considering an alternative business model? Understanding what the drivers are provides essential background about what aspects of performance are most important.
- the perspectives of the different parties within each model. Parties within an agreement may include: business operator, contractor, land owner and investor (joint venture partner). While there may be alignment, generally the different parties will have differing requirements reflecting their personal, business and financial situation.

OTHER CONSIDERATIONS

It is common for the financial performance of farm business models to be considered in isolation, making the potential financial outcomes the primary focus.

However, non-financial considerations should not be dismissed when assessing the potential suitability to personal and business circumstances.

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Case study

CORPORATE-STYLE JOINT VENTURE IN SOUTHERN NSW

Back in 2008 the DB Group was formed by a merger of four family-run agricultural businesses. Rather than pursuing a debt-financed farm growth model, the DB Group chose to operate as a simple limited trust.

The structure provides land access certainty through formal legal arrangements. Each family retains the land they own in their individual names and leases the land to the DB Group, which provides either fixed or variable income streams.

With the assistance of professional advisory firms, the group reviewed the businesses and realised the farming operations needed to scale up and retain their intellectual property. This would reduce the burden of fixed costs and achieve greater efficiencies. However, it was decided that continuing to use debt finance would only increase the financial stress and perpetuate the cycle of farming debt.

DB Ag is the farming entity of the DB Group and owns everything, including machinery and livestock, except the land. DB Ag also employs the labour for growing and marketing the crops and livestock.

To maximise returns and reduce production risk, the properties are spread geographically and machinery and personnel are shared between localities. In addition, off-farm agribusiness arms exist in retail stockfeed and warehousing, and a Pioneer promoter agency and cotton accumulation.

Today the group manages more than 17,000 hectares, with in excess of 13,000 ha of winter cropping sown annually and 5000-6000 ewes as part of its core business.

The business also integrated an additional two families into the ownership structure in 2013 and 2015, demonstrating the flexibility of the model.

Frequently asked questions

What are the main potential benefits from adopting an alternative farm business model?

A successful transition to an appropriate and carefully considered alternative farm business model can enhance profitability, provide more effective risk management (by sharing the risk with others) and assist with business succession, overall providing a more robust and sustainable farm business.

Should an alternative farm business model be considered for enterprises in financial difficulty?

While adopting an appropriate farm business model can help address financial issues, business success also depends on the ability to manage and operate the business well.

The benefits of an alternative farm business model mean the enterprise should be better able to manage adverse times in the future; however, this is not a quick-fix solution. Alternative farm business models may involve additional costs associated with set up and implementation and can take several years before the benefits are fully realised.

Is the 'hand over' phase of a succession plan a good time to implement an alternative farm business model?

Handing over a viable business is the ultimate aim of farm business succession. Implementing an alternative farm business model as part of the transition of business ownership and management allows all parties to have input into the design of the alternative business model, ensuring that the needs of all key people in the business are met.

Useful resources

GRDC GrowNotes – 'Farm business models – options for building your future', www.grdc.com.au/GrowNotes

More information

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References

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