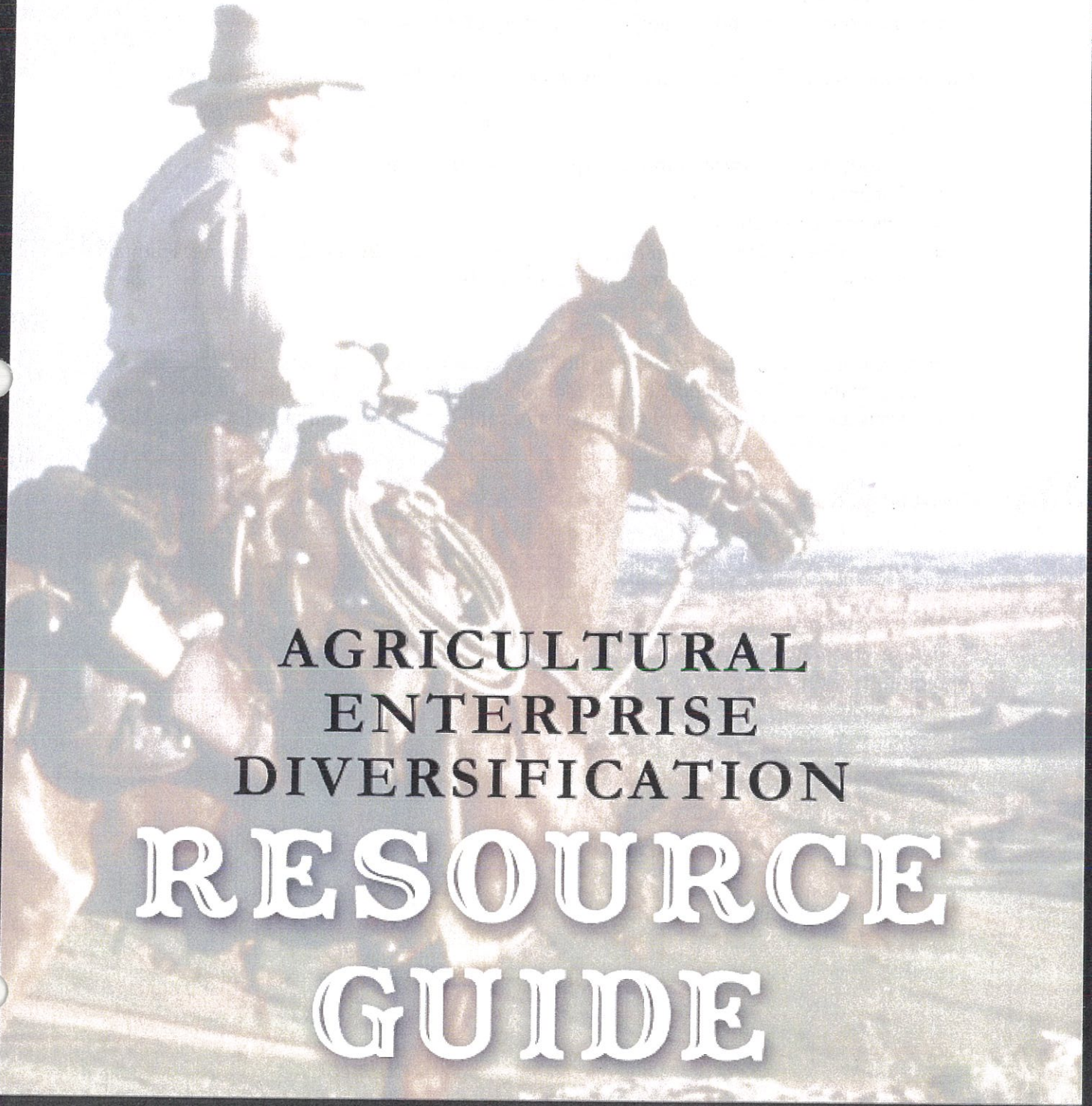




Sustaining Western Rural Landscapes, Lifestyles & Livelihoods



AGRICULTURAL
ENTERPRISE
DIVERSIFICATION
**RESOURCE
GUIDE**

To Whom It May Concern:

The *Sustaining Western Rural Landscapes, Lifestyles and Livelihoods* partnership completed the comprehensive agricultural diversification resource guide as a valuable tool in assisting professionals in delivering technical assistance to agricultural producers as they evaluate their current operations and research the feasibility of diversifying.

The information, at first glance, may look overwhelming, but is divided into the following sections:

- Foreword
- Introduction to Agricultural Enterprise Diversification
- Enterprise Assessment
- Enterprise Feasibility
- Enterprise Implementation (Business Planning, Legal, Finance, Marketing, Human Resources, Natural Resources and Community)

If you would like further information on how to best use this guide please don't hesitate to contact me at the following address. In addition we have access to professionals who can assist agricultural producers develop an agricultural diversification strategy, so please don't hesitate to contact me.

Sincerely,

Cindy Garretson-Weibel

Cindy Garretson-Weibel, Agribusiness Director
Wyoming Business Council
214 W. 15th St.
Cheyenne, WY 82002
(307) 777-6589
cindy.weibel@wyo.gov



A. Introduction

“Where can I find money to start my business?” is the most frequently asked question from entrepreneurs. The most logical place to look for financing is in a person’s own assets. These sources include money in bank accounts, certificates of deposits, stocks and bonds, cash value in insurance policies, real estate, home equity, hobby collections, automobiles, pension fund, Keogh or IRAs and credit cards. One must consider carefully which of these options to choose, as penalties and a loss of interest income may occur. Friends and families represent another source of money. If this is an option, these transaction should be handled in a business-like way with clear terms and agreements.

This section provides information on many alternative sources available to finance small businesses and a brief description of financial statements to prepare before visiting a lender. Keep in mind that each business has its own individual circumstances, location, resources, and goals that will influence the selection of money or financing sources.

1. Why is the money needed and how will it be used

These are two very important questions. Often times, an agricultural entrepreneur, as well as any other individual wanting to go into business, does not completely understand what financing needs they have. One must identify what type of loan is needed, and the intended purposes of the loan.

There are basically four different stages of financing, and a variety of ways to obtain money available for these different stages. The four basic financing needs of business are:

- Seed money
- Startup capital
- Working capital
- Growth capital





Seed money is money needed to develop an idea. It is used for research and development to create prototypes, researching the market and writing business plans. Money for this stage generally comes from personal finances or friends and family. Investors are rarely interested in investing at this early stage.

Start-up capital is used to take the business concept to the marketplace. It pays for initial equipment and all expenses of getting the business underway. Start-up money comes from personal finances, friends, family and sometimes investors and banks, if the concept is very strong and the management team looks good.

Working capital is used for financial inventories, accounts receivable and the cash necessary to operate the business. When a business has a good track record, then working capital is the easiest money to attract. Banks are traditional financiers for working capital and factoring companies also play a major role here.

Growth capital is used for financing expansion, purchasing new equipment, or training new people for the growth of the business. Traditionally, growth is financed by the profits of the operations. Other sources for growth capital include angel investors and venture capitalists, stockholders and taking a company public.

2. **Debt financing versus equity financing**

Debt financing can be defined as any type of loan, where you borrow money and pay the money back plus interest. Banks are not the only debt financing option. Other sources for debt financing include credit unions, cooperative banks (such as The Farm Credit System), consumer finance companies, and insurance companies are just some examples.





Equity financing involves receiving money in exchange for the investor(s) to have part ownership of the business. Examples of equity financing include venture capital investors and angel investors. The following is a list of options for both debt and equity financing.

- An established company or business has several options available to serve financing needs. These include taking a first or second mortgage on any real estate property owned, borrowing money against machinery or hard assets such as equipment or motor vehicles, or borrowing against a pension fund or investment that is considered liquid.
- Commercial banks represent the largest single source for loans and financing. The amount of interest they charge is based on two factors: the size and history of the customer and the risk the bank will take in providing the loan. SBA -guaranteed loans are available through banks, making more money available for business loans.
- Loan companies are considered collateral lenders, meaning they rely upon the borrower's ability to back up every dollar of the loan with assets. Their interest rates are usually higher than banks.
- Credit unions have traditionally financed cars and appliances, however, recently they have expanded their lending operations to include non-members and investments outside traditional financial investments.
- Angel investors may operate as individuals or several individuals who invest together to make investments and loans, usually in exchange for an equity interest in a company. The funds available from private investors vary widely. Investors can be found through local bankers, accountants, and lawyers.
- Venture capitalists almost always seek an equity or ownership interest in the firm in exchange for capital.
- Suppliers can be a great source of funding by giving 30 to 90 day terms. Sometimes, suppliers will provide supplemental equipment that is necessary for use with the products they provide.





-
- If a person leases equipment instead of buying it, he may find companies eager to help make the deal.
 - Local economic development agencies are interested in attracting new businesses to particular areas, and many times offer significant incentives. Check with the local economic development agency or with the Wyoming Business Council for details.
 - For small loans, the Wyoming Women's Business Center provides loans for up to \$2,500. WWBC partners with other financial institutions and economic development agencies to provide these loans.
 - The Wyoming SBIR/STTR Initiative, more commonly known as the SBIR (Small Business Innovative Research) program, is a federal research and development grant or contract program specifically for small businesses. Through the SBIR program, 10 federal agencies provide more than \$1 billion in research and development funding annually. This is a three-phase program in Wyoming. The phase O program provides \$5,000 for preparation and submission of a specific SBIR Phase I proposal. Phase I proposals are a feasibility study to evaluate the proposed project's technical merit for which an awardee may receive a maximum of \$100,000. Phase II proposals involve research and development efforts that expands on the Phase I competitive program that funds new, innovative new commercial products or services. The money is a grant and is not paid back, although complete and accurate records must be maintained on expenditures.
 - There is also the possibility of owner financing if buying a business. Ask the seller if he or she will be willing to sell it to you on contract.
 - The Small Business Administration offers loan guarantees to commercial lenders making loans to small businesses for working capital, inventory, machinery, land, buildings, purchases of businesses and other "new money" projects.





3. Successfully obtaining financing

The best preparation an entrepreneur can do to obtain financing is to prepare a complete business plan. A common mistake is to seek financing without a written plan. As the entrepreneur or business owner puts the information together for the business plan, they should keep in mind the validity of the information gathered. Lenders will have more confidence in lending if they feel the information presented is supported by documentation and the information is gathered through credible resources.

Loan requests are evaluated on the *Cs of credit*. A lender will look at all of these areas. Some are more crucial than others.

- *Credit* – A credit check will be made to look at references, credit report, liens, delinquencies, and bankruptcy.
- *Character* – A lender has more confidence in a borrower who is honest, and in good standing in the community.
- *Capacity* – Capacity is the ability of the business to generate funds and repay the debt. A lender will also look at secondary sources to pay the debt back.
- *Collateral* – Lenders want to make sure they get paid back, and want to know what assets a business can use to assure the debt is repaid.
- *Conditions* – Conditions include both the economic conditions at the local, state and national levels, and also the economic conditions within a specific industry.
- *Capital* – How much money is the business willing to invest? Lenders will not loan 100 percent of financing needs.

The entrepreneur should view the lender as a team player and approach all interactions with a professional attitude. Refer to the business plan sub-section of this resource guide to understand the elements included in a business plan. Once the business plan is written, the lender will also ask for:





-
- Three years of personal tax returns
 - Three years of business tax returns, if applicable
 - Appraisals on all properties (business and personal)
 - Personal financial statements of all owners
 - Lenders usually run a complete credit check on all owners/borrowers

4. **Financial statements**

Financial statements provide small business owners and entrepreneurs with the basic tools for determining how well their operations perform at all times. Many small business owners do not realize that financial statements have a value that goes beyond their use as supporting documents to loan applications and tax returns.

These statements are concise reports designed to summarize financial activities for specific periods. Owners can use financial statement analysis to evaluate the past and current financial condition of their business, diagnose any existing financial problems, and forecast future trends in the businesses financial position. Virtually all suppliers of capital, such as banks, finance companies, and venture capitalists, require these reports with each loan request, regardless of previous loan history. Also, prospective buyers of a business will ask to inspect financial statements and the financial/operational trends they reveal before they will negotiate a sale price and commit to the purchase.

Forms that are essential to prepare before seeing a lender include:

- Income statement
- Balance sheet/pro forma balance sheet
- Cash flow

The two key reports for all sizes and categories of business are the balance sheet and the income statement. What do these forms tell the lender?





The balance sheet is an itemized statement that lists the total assets and the total liabilities of a business, and gives its net worth on a certain date. The preparation of a balance sheet or future projections is called the pro forma balance sheet. Pro forma balance sheets are used to project how the business will be managing its assets in the future. For example, a pro forma balance sheet can quickly show the projected amount of money tied up in receivables, inventory, and equipment. It can also be used to project the overall financial soundness of the company. A pro forma balance sheet can quickly pinpoint a high debt-to-equity ratio. This statement provides two views of the same business: what resources the business owns, and the creditor and owner investments that supplied these resources. These divisions are generally set up in the two-column account form, with assets on the left, liabilities and equity on the right. An alternative – the one column statement form or report form – lists assets on top, liabilities and equity below.

The income statement, also called the statement of income and expense or profit and loss statement, records revenues versus expenses for a given period of time.

Cash flows fall into two categories: inflows and outflows. Inflows include revenues from sales, proceeds from loans, and capital injections by owners. Outflows include costs of sales, operating expenses, income taxes, repayment of loans and distribution to owners. The cash flow statement will also show the break-even point. The break-even point is basically when cash income equals the cash outflows.

There are many ways to finance a business, and there are many more options available than listed here. One should think creatively and possibly look at combining several options to obtain financing to grow a business.





5. **Resources**

“Tilling the Soil of Opportunity...NXLevel Guide for Agricultural Entrepreneurs,” University of Colorado at Denver, University of Nebraska and US West Foundation, December 1999.

“Wyoming SBDC Business Counselor Certification Training Manual,” Wyoming Small Business Development Center, Laramie, Wyoming 2000.

