



Center For Agribusiness & Economic Development

Value Added Enterprises

Chris Ferland, Brigid Doherty, Nancy Dykes, and John McKissick

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The Center for Agribusiness and Economic Development is a unit of the College of Agricultural and Environmental Sciences, combining the missions of research, teaching and extension. The Center's mission is to inform the public and private sectors of the importance of Georgia agriculture and assist in increasing the value of Georgia's agricultural economy with value-added products, new processing, and packaging. This paper suggests tools and ideas on how to get a new enterprise started and running successfully. The first part of the paper explains the importance of agriculture to the Georgia community. The paper then shifts directions to basic business ideas and plans for any new venture. Concluding the paper is more information on the Center for Agribusiness and Economic Development.

Value Added Enterprises

In recent years Georgia agricultural producers have been fighting high input prices and low output prices that negatively affect the rate of return to the farm. Opportunities may exist for some farmers to add value to the commodities they produce and thereby increase their return. Farmers, extension representatives, agribusiness and entrepreneurs can use the Center's knowledge and research base to explore and exploit opportunities that exist in value added products, marketing, and packaging through the following mediums;

- Economic/Financial analysis
- Feasibility studies
- Marketing plans
- Market research and distribution
- Strategic plans
- Research publications.

Producers and entrepreneurs looking for alternatives to traditional agriculture do not always have the resources to investigate their ideas. The Center will provide assistance in researching and implementing these ideas to reality. Projects are reviewed and considered by their potential impacts. An application must be completed and submitted discussing the project and information needed.

Georgia's Agricultural Economic Impact

Agriculture in Georgia is as important as water to the human body. Once a person gets out of the metro Atlanta area the landscape opens up with pastures and livestock. Get a little further out from the city heading south and large fields appear full of agronomic crops.

When one adds all the components of agriculture together in Georgia the importance of the industry become overwhelming. Food manufacturing, distribution, forestry products, agri-tourism, and fruit and vegetables also increase the importance of agriculture.

In 1999 the total farmgate gross income of agriculture and forestry in Georgia was \$7.83 billion in 1999.

The top seven commodities were:

1999 Farmgate Value by Major Category

Grouping	Value	Percent of Total	Rank
Poultry and Eggs	\$3,337,268,837	42.11%	1
Row and Forage Crops	\$1,342,844,240	16.94%	2
Livestock & Aquaculture	\$852,360,542	10.75%	3
Forestry	\$737,071,537	9.30%	4
Vegetables, Fruits & Nuts	\$691,510,480	8.72%	5
Other Income	\$548,776,073	6.92%	6
Ornamental Horticulture	\$416,188,461	5.25%	7

Georgia's economy was worth \$352.8 billion in 1995. Of this agriculture (including food and fiber processing) represented 38.9 billion (11%) and forestry (including wood and wood fiber processing) represented \$17.8 billion (5%).

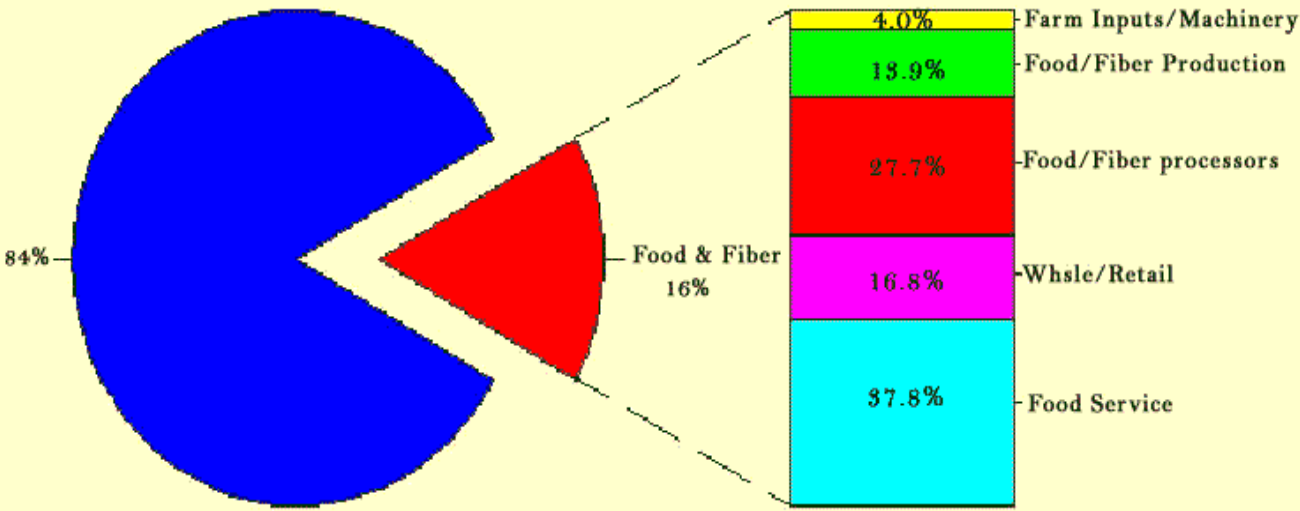
The total work force in the food and fiber sector (agriculture and forestry) is an estimated 650,000 currently, making up 16% of the Georgia workforce (473,000 in ag; 177,000 in forestry).

In 1996, farm assets in Georgia were worth \$18.5 billion. The 1998 total estimated value of standing timber in the state of Georgia is \$31 billion.

As one can see agriculture in Georgia has an impact on life in Georgia but also other area of the world. The Georgia Agricultural Statistics Service has export value for 1999 at \$866.8 million.

1995 Georgia Total Employment: 4,204,763

Food and Fiber Output: 634,941



Understanding that agriculture is important to Georgia allows one to appreciate the efforts incorporated by farmers attempting to adapt to the shifting world economy and price fluctuations. One aspect assisting farmers in receiving higher returns is adding value to their products. Some farmers produce jellies, jams, onion relish, grow high oil grains, bottle their milk, or open fresh produce stands. Any time one adds value, whether it be by delivery, packaging, or service a premium can be expected for the product. Peanut and fruit growers have been expanding business from a local market to world market by utilizing the World Wide Web. Growers of ornamental crops also advertise with web sites.

Part of the move towards value added products derives from farmers wanting to capture more of the retail to farm price. The chart below shows the decreasing trend in the amount per dollar the farm receives from the retail market. To increase the amount received, many farms have been marketing their products in the retail market themselves.



As an example consider the conversion of wheat to bread. A bushel of wheat produces over 100 loaves of bread. The farmer sells the wheat for \$2.40 a bushel and the consumer purchases the bread for an average price of \$1.50. The farmer receives approximately \$.016 per loaf. This spread between the raw material and finished good is referred as the "farm to retail spread". The spread has increased the last few years. When the raw commodity price drops, as it has, and the finished product remains at a constant level the spread widens and pulls the farmers financial statements downward. Due to this widening of the spread the importance of value added has grown to the farm base. Thus why farmers are preparing and packing commodities directly into the market. They need to enter and gain market share in order to receive some of the "farm to retail spread" at the farm level.

Beginning a New Venture

To begin any new venture, a producer needs to sit down with the family and others involved in the daily business and write down all ideas and possibilities. Even if the idea may seem unrealistic, write it down and research the market. Many people open produce stands or start ventures without researching the market potential. A fresh produce stand located on an un-traveled road makes no sales.

The following sections are brief descriptions of tools often used when starting a new enterprise or business. These paragraphs are only a guideline and do not guarantee success.

Goals

Every business needs to have goals that are simple, consistent and long term. The producer should not enter a venture without believing what he/she is doing and having goals for measurement. These goals come with an understanding of the environment entered. You need to know the enemy before you can begin the battle. Sizing the battle up before entering proves to be an effective way of learning. Then one can exploit their strengths while protecting their weakness. If you know your crop yield is consistently above the county average use that to your advantage. Accessing and employing our comparative advantage benefits the business by fully utilizing the strengths. Produce as many as possible efficiently. If your business skills are weak do not be afraid to ask for advice. Pride does not always belong in the family business when making decisions. Finally, effectively implement the strategy calculated to obtain the goals stated in your plan.

Vision

Visions create a sense of purpose for the employees and owners. They allow connection of the employees to success. In conjunction with visions one should have mission statements. Mission statements link the vision and strategy together into one paragraph. This communicates the business' values, vision and means to obtain them into a plan or one primary objective.

Resources

The farm needs to analyze its resources. Only after knowing what you have can you begin to plan for the future. Knowing your resources allows you to utilize your capabilities to the maximum. The strategy of the firm is to employ its resources into the industry environment. Each business type, location, and maturity exists in different environments and before a firm can be successful they need to explore and discover their environment. Analyzing the environment opens the doors to the competitors that exist. Your most dangerous competitors are those similar to you. "Good analysis should encourage the development of intuition and promote creativity" (Grant, 1998).

Projected Cash Flows

After an idea is set and the business knows what resources it has, a projected cash flow should be assimilated. One idea that needs to be understood is that when preparing projected cash flows one is forecasting into the future, which can cause difficulties because no absolutes are known. The projections are based off actual figures and uncertain perceptions for future performance. The cash flow should be used to see if the company could fund itself during a certain time period, at least through start up and the life of the asset employed.

Barriers to Entry

Be aware of barriers to entry. Many of the enterprises an agribusiness may dream of have barriers. Some come in the form of packaging requirements with the USDA. Other barriers will be regulations protecting consumers on the state, federal and local level: health stipulations, weight and measurements, meat inspections, labeling and workers rights. Be sure to research this arena and get all information possible.

Insurance may also be a barrier to entry. Liability insurance is a necessity in today's world with any product or service offered. Even pick your own places need to insure against liability. Certain organizational structures can reduce the amount of insurance needed. One example is the asset structure set up in the business. Some businesses keep the asset as personal items, but rent them to the business. This protects some of the assets from liability cases. If the firm is set up as C corporation or sub chapter S corporation this scheme works well for protecting the personal assets from lawsuit. It is important to consult with a lawyer and an accountant about your business structure annually.

Product Differentiation

In a world of competition, one weapon effectively used is product differentiation. Niche markets are an example of this theory. Product differentiation is taking a product and making it different than others. This application also helps establish a brand name. Some agribusinesses have made hot pepper salsa and local wines. These products may appear to be similar to a store bought brand but are different on many levels. One, the produce was grown locally, bottled locally, marketed in a different fashion, and probably contains different ingredients. Wine in the South is made from Muscadines predominantly and not from traditional vineyard grapes, which gives the final product a different taste, smell and pleasure.

Distribution Channels

Probably one of the hardest items for a new agribusiness venture to overcome is the distribution issue. Gaining shelf space in the retail market is difficult and sometime highly unlikely for a newcomer to achieve. Shipping the products in large quantities is also a problem. This issue has been shrinking with more people creating their own shelf space via the Internet and shipping with UPS as soon as the web order is placed.

Retaliation

Any effectiveness into a new venture depends on the retaliation by competitors. Already established competitors may be able to undercut a new business by lowering prices or squeezing suppliers. This is typically seen with larger firms but can exist on any level. An example was when American Airline reduced their tickets prices by 50%. Starter airlines, such as Southwest, protested saying American was undercutting them. This was done in attempt to drive them out of the market. The government found in favor of the small airlines. U.S. soft drink producers such as, Coke and Pepsi, often undercut new entrants into their market.

Demographics

This could be the most important aspect that needs to be examined for any business. Who are they marketing the product towards? If the company markets to the wrong group, failure is inevitable. Demographics are composed of the stratification of the population into smaller groups, either by age, class, education, attitudes, marital status, or almost anything. Take for example Ford's new Focus model is aimed at the twenty something demographic crowd. The commercial has a group of twenty years olds exiting the car with the loud alternative music playing. The business needs to decide what target population they are going to advertise and market their product towards.

Fore Thinking

Every business needs to be a forerunner in the industry. This comes by leading the customer to what they fell they need and want. Delivering products for the future involves using ones core competitive to build gateways to future needs. This sounds a little theoretical but it is really easy. If you make a commitment to producing something even before you produce it you have a higher degree of success. Do not be afraid to market or create new products. The more different they are from other products available but fit an existing need the more successful you will become. The core competency involves not only your talents but also everyone else's you work with and learn from during the years, an integration of skills. Hamel and Prahalad (1995) state a company surrenders business if it becomes more efficient without getting different.

Financing

There are many ways to finance a business. Leverage can be useful in may circumstances. Debt at a lower interest rate then the possible return can play in favor of some finance structures. Financing includes the business structure. Some farms are set up as sole proprietorships, corporations, sub chapter S, or partnerships. The structure needs to be investigated to see which will be beneficial to the individual. No two farms have the same requirements and needs. Financing does not only have to be with the business' retained earnings and borrowed money. Many businesses have been going into the contract side and having the contractor supply their inputs. Others use outside investors to reduce the risk on their equity. The point is a number of different opportunities exist. Variable loans versus fixed loans depend not only on the interest rate but the amortization schedule, termination date and need for funds. The financing and organizational structure good for your business depends on your risk attitude.

A variety of different methods exist to evaluate the profitability of the new venture. Some of the most common methods for evaluating new projects used are Net Present Value, Internal Rate of Return, and Annualized Budgeting.

Summary of Tools

Even knowing how to use all the above to your benefit does not mean the business will succeed. Starting a new enterprise is similar to choosing stocks. The fundamentals may appear strong but historical data does not predict future success. However, the more you know about applying what you have learned the better the probability for success. Differentiation appears to be an essential part of the agribusiness environment. Location also seems to be important. The tourist areas and scenic drives have a greater potential of success with roadside stands and agri-tourist services. But these tourist areas may not be good for ventures such as butcher shops or hog farm tours.

Business Plans

Moving from the traditional production process to the service and value added enterprise requires different skills than just production talents. Some skills needed to run a new enterprise are an understanding of tax laws and labor regulations, accounting skills, marketing skills, budget management skills and people skills. Those people who do not enjoy interaction with others may want to stay on the inside of the operation. People skills are extremely important when dealing with the value added and service industry. If you have any hesitation you may want to think about a different market.

Business plans construct the highways for the owner to travel upon to reach the desired destination. Meaning the plan is the roadway system in achieving the goals of the business (profits). These plans have many different avenues; some roads lead to accounting methods, others to processing efficiency, and still some to delivery on the market place. This map-like plan allows the owner to see where the potential weakness may occur and strengthen those accordingly.

These plans show the start up cost and yearly cash flows needed to run the business. The plan illustrates the operation tactics of the proposed business. Small business retention rates during the first year are less than 60%. This gradually decreases over the next five years. Many unsuccessful business attempts blame the failure on one of two items, lack of planning or lack of capital. Neither reason should happen if one utilizes the business plan properly. These plans exemplify a running business and should touch on all possible problems.

Business plans also serve as tools for the lenders to the business. The lenders often rate business success on the planning side before the operation even starts. Some lenders may even lower interest rates or provide lines of credit to those with highly detailed clear plans. A major key to the plan is pointing out the strategy. Strategy is matching the business's resources with opportunities.

Plans will often include projected cash flows, economic analysis, market demand and growth, financing, and growth ideas. Some key fundamentals of a business plan are:

- Why am I farming and what do I want to accomplish (What are my goals?)
- Are my goals obtainable with my vision and values?
- What are my core competencies and weaknesses?
- Where does my competition exist?
- What other industry can I benchmark against and borrow technology? (It is good to get out of your industry and look elsewhere for ideas)
- Where will the financing come from and does it cash flow?
- What market should I attack?
- Develop and evaluate strategies to be applied.

This plan needs to examine the external environment and the internal components of the business, revealing to the owner and operator the potential areas for improvement and areas that need to be taken advantage of for future profits. Business plans are cyclical and need to be monitored and evaluated on a yearly basis. The business needs to apply the plan in all decisions made. Even the simplest of decision affects the overall outcome of the farm business. Patience is required for it will take some time to get used to thinking in this fashion.

Marketing Plans

Business structures are like three legged stools. Each leg supports the business and when one leg is weak the stool wobbles. This paper briefly has covered two of the legs already, finance and operations. The business plan deals with both of those. The final leg is marketing. Marketing for value added is not exactly the same as marketing for traditional agricultural products in the sense of risk management. Marketing encompasses four key components often called the four P's: Product, Promotion, Price and Place.

A product is the tangible and intangible listed for sale, such as the organic foods or the service provided, butchering. Products need to be differentiated from their competitors. If the items for sale are not unique or provide additional service, the sales are based upon price. To gain customers and create name recognition, offer a product not a commodity. Distinguishing yourself from similar products will attract potential sales and develop brand name recognition.

Examples of differentiation can be seen throughout retail business. One of the most common is packaging. When the dairy industry switched from the square cardboard boxes to the twist off cap on the plastic bottles, milk sales increased. This was a simple packaging tactic. Other ways to add value to a product besides packaging is service. Free delivery, assembly, hotlines, free consultation, are all services that add value (a premium) to the product being sold.

Promotion is the next component in marketing. Promotion begins as soon as the customer walks in the door or asks a question. The relationship being built here can have direct impacts to the decision to purchase an item or not. Satisfied customers talk about their experience and you gain valuable promotion. Unsatisfied customers also talk. Emphasizing the customer relationship in itself develops promotion and brand name for the business. Marketing to the correct demographic section also promotes the product. The business needs to investigate the environment and know whom they wish to target the product towards. Targeting the wrong sector wastes resources and time. The more precise you can target the product the more successful the marketing scheme and the greater potential for increased sales.

Location can be a determining factor in the success of the product. Place should be a location near the targeted audience, or it can be over the Internet, in a catalog, or type of retail shop. Place is important because if buyers have to search too hard to find the product they may purchase a complementary item instead. Relative ease for the target population should be considered when selling the product. Complimentary locations work well for products. Have you ever notice that in the mall most of the men's stores are located relatively close to one another? Brookstone is usually only a few doors down from a men's clothing store, which is close to the outdoor gear store.

Price, the final P, is based off the equilibrium of supply and demand. If prices are too high, consumers buy alternative products. If they are too low consumption will be greater then the supply creating a deficit. Value added and services provided need to be included in the price. These typically add a slight premium over total cost and return to management.

Using the 4 P's and the business plan, one can create a marketing plan. The information needed from the business plan are the operational numbers, quantities of product to be produced, and projected cash flow. When developing market strategies, one needs to create benchmarks for the quantity of products to be sold in the certain market segments.

Benchmarking allows the business to appraise the organizational capability and compare themselves with similar businesses. The benchmarking criteria includes: locating a section of the business were there is a potential for improvement, finding and comparing yourself with the business that leads in the activity, analyzing the differences in that activity and using what you have learned from the comparison to improve.

After benchmarking and improving, the business can develop marketing strategies. These strategies act as the outline for each individual product. This outline form includes the objectives of the firm, predicted amount of sales, method of obtaining the market, and the formula for success. The biggest issue to each plan mentioned in this paper is implementation. A plan is no good if it is not followed and implemented.

Success

Farmers over time have concentrated mainly on production efforts and becoming efficient in production. This production efficiency has aided farmers in dealing with the shifting consumer market, government policies, and world demand but it has not made too many farms more successful. What the efficiency has done, at certain time periods, is provided excess working capital or space for maneuverability during the slow times. The economy and farm structure have been changing but the efficient operations do not appear to be adapting at the same pace. Even with low crop prices, farmers have used their efficiencies to produce more. Contradicting economics, the efficiency thus creates a greater supply and keeps the prices low. As one can see success is not always associated with efficiency.

Success should be thought of incrementally. Moving towards the business goals by following the vision in small steps is acceptable. Think of success as a stairway to the top, every floor climbed places you closer to the goals and plots your progress. Good feelings will stem from forward progress and motivate for future forward movement.

There are many ways to measure success in an operation, financial market penetration, and expansion. One way to measure success is through asset management reflected on the balance sheet and financial ratios. The other way is operational management reflected on the income statement and operating efficiency. These two methods are only slightly tied together. One can have good operating efficiency but low return of assets.

Again, success should not only be measure as efficiency or profitability. Growth and opportunities for further success need to add into the calculation. Many businesses have been successful but they do not seem to hold that success for lengthy time periods. Success should be the business that can identify opportunities and take advantage of them on a regular basis.

The Center for Agribusiness and Economic Development provides the analysis necessary for the decision on whether to enter the value added market. A fine line exists between adding value and losing money. The market creates the price by the balance of inputs, outputs, and competition. Experienced and professional staff will undertake a full analysis of the project and a written report is produced at the end of the study. The information in the report should be substantial enough for the entrepreneurs to decide whether to go ahead with the project or let it lie.

The Center issues press reports and special reports regarding agriculture in Georgia. The annual Farmgate report is prepared and disseminated by the Center as well as an array of reports. It is the position of the Center to publish reports based of the general information of any study completed.

Agriculture is a major player in the Georgia economy. The Center's goal is to improve the recognition of agriculture and assist those involved in its production. Feel free to contact the staff of the Center of Agribusiness and Economic Development at 706-542-0760 or fax inquires to 706-542-0739.