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FACT SHEET

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MANAGING CREDIT IN AGRIBUSINESS

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Managing the total credit needs of an agribusiness firm requires careful attention to both sides of the credit picture — that secured and that granted. Better use of operating capital results when a firm's management carefully reviews periodically its credit policies. During periods of tight money this review is imperative, if agribusinesses are going to remain competitive. This publication discusses briefly credit management guidelines suitable for agribusiness firms.

CREDIT-SECURING POLICY CONSIDERATIONS. Agribusiness firms secure operating credit in two ways. Negotiating loans from financial institutions is one method; the other is securing credit from suppliers.

- Items of utmost importance in selecting the lending institution from which to borrow operating capital follow:
  - Competency of its staff to advise agribusiness firms in management decisions.
  - Services provided its business borrowers. Do they assist in preparing budgets and cash-flow analyses?
  - Costs incurred by borrower.
  - Lender's attitude toward the type of agribusiness requesting the loan.
  - Lender's reputation in staying with a borrower when the going gets rough.
  - Extent to which it can meet short-term, intermediate and long-term agribusiness needs.
  - Cash-Flow Budget

Most agribusiness firms want to manage credit in such a way that ample operating capital will be available when needed without having idle funds. This can be accomplished only with cash-flow budgets.

A cash-flow budget is a monthly or quarterly portrayal of a firm's planned income and expenses. When projected for a year, these monthly or quarterly breakdowns reflect operating capital surpluses and shortages. Such a budget permits borrowing only needed funds when they are needed. Firms that can present to a lender well-prepared cash-flow budgets usually encounter minimum difficulty in securing loans.

- Select a supplier after careful evaluation of the following:
  - Price and quality of its product.
  - Its credit policy which includes service or interest charges and early-pay discounts.
  - Services provided its dealers. Does it assist in advertising, display, accounting procedures, sales training, etc?
  - Dependability. Can it be counted on to fulfill its commitments?
  - Convenience to dealer.

CREDIT-GRANTING POLICY CONSIDERATIONS. A proper decision concerning the granting of credit to its customers can be reached only after a firm's management compares the advantages and disadvantages of credit extension.

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Advantages to granting credit.

- A more personal relationship results with the customer.
- Credit customers are more regular. They are less likely to be bargain hunters as are cash customers.
- Quality and service are of more interest to credit customers than is price.
- Goods can be exchanged and adjustments made more easily.
- A roll of credit customers provides a permanent mailing list for special promotions.
- A study of credit customer accounts indicates buying trends and habits.
- Sales are more easily made.

Disadvantages to granting credit.

- Working capital is tied-up.
- Pricing must include interest on capital tied-up in accounts receivable.
- Losses from bad debts.
- Inclination on the part of some credit customers to overestimate their ability to pay.
- Abuse of the privilege of returning goods.
- Additional overhead expenses are incurred in administering credit accounts.
- Increased demands on management.

If the policy is to grant credit, these features are essential:

- A definite procedure for checking references before extending credit to a customer.
- A thorough understanding with the customer as to the amount of his line of credit.
- Clearly stated terms of sale to include the amount of service charges or interest rates, if any. Plan for payment by customer should coincide with his receipt of income.
- The maximum accounts receivable a firm can carry without jeopardizing its financial position.

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