

GOOD DECISION-MAKING TIPS FOR YOUR BUSINESS

- Good business models – general principles
- Where to start when setting up a business
- Good decision making, complexity/uncertainty etc
- End story: Why some small businesses fail (avoiding the pitfalls)



INTRODUCTION

In agriculture there are exciting opportunities and significant risks. In order to deal with both, you must apply skills in the technical aspects of your enterprise and in managing your business and its people. If you do not have the required skills, you need to develop them or outsource the job.

When you examine the key elements of successful farming businesses throughout Australia, there are some recurring themes, principles and rules of thumb that can help farmers in considering and assessing their businesses and business decisions.

This information sheet provides tips on setting up and running a successful farming business. It lists questions that need to be answered as you develop your ideas, and shows how to avoid some of the common pitfalls for small businesses.

Information in this document has been produced as a guide to good business decision making and does not constitute sound financial advice. Professional advice should be sought from an accredited financial advisor.

A SOUND BUSINESS MODEL – GENERAL PRINCIPLES

Small farming businesses are usually driven by passion for what people do. You need the passion but it must not distract you from sticking to the key elements in any good business model.

Here are some tips:

- **Make a plan** – be clear about where you are now and where you want to be with your business and your life, be realistic about what you can do within your budget within a certain timeframe; review and adjust your plan every 6 months.
- **Get advice** – good advice can help you avoid making basic mistakes; you cannot know everything.
- **Know and build a market** – spend time talking to buyers or potential buyers, understand what they want and then produce it for them. Start close to where you are.
- **Maintain a market** – work with your market and ensure you are a supplier of choice and can give your suppliers what they want and when they want it.
- **Know the numbers** – know what your costs of production are and what the market is prepared to pay; identify how you can improve efficiency to have a sound margin.
- **Manage the risk** – write down what your risks are and how to manage these to maintain sanity and good returns.
- **Expand the business step by step** – once the initial steps are in place there is potential to expand if the market can grow and you have time, money, energy and a good plan. Know what the market wants and know the parts of your business that are profitable.

There is no 'right or wrong' recipe, but these points can help you think it through, ask questions and discuss with others.

SO – WHERE DO YOU START?

You may have loads of great ideas. To take the next step, you first need to be honest with yourself and ask some important questions about what suits you and why you want to start or diversify your own farming business and who wants your product.

Having the courage to try something different and 'just doing it' cannot be underestimated. Many people do not ever develop their ideas because they just never get started; others start too many things and never finish or do any of them well. Success in any new enterprise is possible provided you do your research first, plan carefully, have the finances to survive the first tough years, and you are prepared to put in the hard work required.

The first steps involve choosing the right idea or business for you and then conducting enough research to ensure that your idea is feasible.

CHOOSE THE RIGHT IDEA FOR YOU

- Are your expectations realistic?
- Do you have a passion for what you plan to do?
- What is your long-term vision?
- Do you have the right skills? Is there a market for your product or service?
- Do you have the funds?



Don't be afraid to seek out technical, marketing or financial assistance or training courses, if you do not possess skills in these areas.

IS THE LAND & CLIMATE SUITABLE?



Photo: A. Renkin

Be realistic about the suitability of your land and location.

Whether you are starting a vineyard or a sheep dairy, there are certain environmental characteristics to consider.

PART OF YOUR EARLY RESEARCH REQUIRES ANSWERING THESE QUESTIONS (IN SOME DETAIL):

- What types of soil do we have and what level of soil fertility do we need?
- Are our soils sensitive to salinity or sodicity (and therefore needing careful management)?
- Are there water quality or quantity limitations?
- Is there good drainage?
- Will our olives/pastures/berries grow in this climate?
- Are slopes or stones a problem?
- How can we manage or reduce any of the above limitations?

Aim to determine what enterprise you can successfully manage, either by looking at what else is grown in the area or by investigating the soil, water and climatic requirements of your desired product.

DO YOU HAVE ENOUGH FUNDS & TIME?

It may take several years before you are able to generate a return from your investment, particularly where there is a significant establishment period such as with olives, grapes or other horticultural crops.

Do you have sufficient funds or alternative sources of income while waiting for these to mature? Even when established, do you have sufficient resources to allow for market fluctuations? Can you 'weather the storm'? Be realistic, allow for some degree of failures in your financial planning for the first years. Try to spread cash flow over a long period, if possible.

Whatever your enterprise, start small so that you can learn and so that mistakes are not too costly. Plan expansion and diversification carefully. Investigate whether you can contract out certain activities to save time.

Financial success can be dependent on having adequate finance to fund you until your enterprise is fully established and generating the profits you initially planned for.

IS THERE A MARKET?

Find out early the level of demand for your product. Statistical and other market research data (e.g. from ABS, ABARES and trade publications) can help you make an informed decision.

Talk to potential customers, other local businesses or wholesalers. Analyse your competitors – how many are there and what are they doing? What segment of the market will you target? In general, it is more profitable and sustainable to establish and occupy a niche in a market than to offer a commodity and compete with others on price. It is also helpful to understand market trends so you can make the most of your business opportunities. How healthy is the market? Is there room for further expansion? What is the volatility of the market - if there is an increase in the volume of product within the market will the price go down? What are the costs of bringing your product to market? Starting small and close to home will help in getting it right.

WHICH BUSINESS STRUCTURE IS RIGHT FOR YOU?

A business structure is used to identify your operation as a trading business.

It is an important decision, and you may need qualified legal, financial or business advice to help you choose between sole trader, partnership, company and trust. Each has advantages, disadvantages and responsibilities of which you need to be aware.

THE FOLLOWING QUESTIONS SHOULD BE CONSIDERED:

- Who can make important decisions?
- What are the tax advantages and disadvantages?
- Is it inexpensive and easy to set up, or complicated and perhaps expensive?
- Can I change the structure easily?
- What are the legal obligations e.g. what records do you have to keep?
- How are profits (or losses) shared?
- How easy it is for the business to expand or attract new investors?
- Do you have investors / a board of directors you have to consider?
- If your business is a family owned and operated one, do you have a good separation of tasks and a succession plan?

Choose a business structure before you start your business so you can comply with the various legal requirements it carries. Ensure it suits your business and family, and manages risk and tax liability. Importantly, seek advice from a professional.

RULES AND REGULATIONS – YOUR RESPONSIBILITY!

Apart from the rules and regulations pertaining to any business, food producers have their own requirements.

Make sure that you understand all aspects of essential record keeping, registrations and accreditations as well as the associated costs for quality assurance, food safety, safe use of chemicals, environmental management and intellectual property.

Understanding legal requirements and regulations is **your responsibility**. Make sure you research it well when planning your business.

NOW YOU ARE UP AND RUNNING – BUSINESS MANAGEMENT TIPS

PLAN - DO - REVIEW

This principle can provide an easy checklist to ensure that your business continues to run smoothly, adapts to new challenges, and identifies opportunities for innovation.



Prepare annual operational plans alongside your annual budget and apply the plan-do-review check to see if you're on track and make changes as needed.

TO ENABLE CONTINUOUS IMPROVEMENTS, YOU MUST:

- **Keep good records**
This includes financial and operational records (farm inputs, timing, weather, yield, soil tests etc).
Take photos to illustrate descriptions.
- **Actively pursue feedback**
Most customers won't provide this unless you ask them!
- **Review the business regularly**
Step back and critically review how things are going. Don't be afraid to seek external opinions or professional advice.
- **Be flexible and adaptable**
Sometimes obstacles are out of your control. Always be ready to listen to feedback and be able to make improvements.

BE ALERT TO OPPORTUNITIES

Don't be afraid to ask lots of questions! Can we work more efficiently? Can we access new technologies to improve our systems?

Can we access improved animal genetics or plant varieties or new agronomy information? Can we improve our service to clients to make it easier for them to deal with us? Are there improved payment options or on-line sales we can implement? Do we have the latest accreditation for quality assurance? Do we need a new system for tracking finances?

PREVENT FAILURE – MANAGE RISKS

To keep your business running smoothly you will need good market, technical and business information to manage risks.

Managing risks requires making good decisions based on an understanding of your risk factors and interactions between them.

CAREFULLY THINK ABOUT:

- What are my risks and risk factors? What can go wrong?
- Which preventive action/s can I put in place?
- Which corrective actions are possible, if something has gone wrong?

To be successful in business you will need to manage risk by using and accessing, analysing and synthesising information. Use your insight, instinct, awareness and discernment to make good decisions.



MAKING GOOD DECISIONS

This fact sheet has hopefully prompted you to consider many different questions as you start or diversify your own farming business.

There are lots of decisions to make. Decisions can be classified as simple, complicated or complex. While we may make hundreds of simple (and some complicated) decisions every day, in business, success tends to come to those who get the big, complex decisions right.



COMPLEX DECISIONS ARE THOSE THAT:

- Involve a high degree of risk and uncertainty
- Incorporate people issues including social pressures and our psychological preferences and/or failings
- May have been simple, but have become complex due to a lack of good information about choices and or too many choices

RISK & UNCERTAINTY

Farming involves the continual assessment and management of risk and uncertainty. Risk is the source of above average profits as well as losses.

In farming, there is the *business risk* that relates to the operational side of running the business, and the *financial risk* that relates to financing the business. There are also risks related to people, you, your family and your staff.

Business risk and uncertainty includes the full range of production, market and price risks. The main sources are variability of weather and variability of prices after production decisions are made and implemented.

People risks include attitudes, stress resistance, knowledge and skills; employers have legal responsibilities but also must be able to relate to and manage staff.

Financial risk and uncertainty refers specifically to the amount of debt a business has relative to the equity (i.e. what proportion of other peoples' money you use to fund the business relative to your own money – gearing ratio) and the effect it has on the rate of growth or decline of a business. The higher the ratio, the higher the risk.

Robust Decision-Making

Robust decision-making requires a risk management approach to decision-making, by enquiring into the uncertainty of a scenario, i.e. what type of risk are we dealing with? How does the uncertainty impact upon our desired outcome? How can we deal with undesired outcomes? A decision can then be made to cope with a variety of futures.

A ROBUST DECISION (OR SOLUTION) IS ONE THAT:

- Remains viable under the widest range of probable scenarios
- Increases flexibility and provides options
- Fits in with other proposed actions
- Does not make you feel stressed

Remember that risk is subjective, experienced differently by different people. You must consider risk and uncertainty from your personal perspective in a way that makes sense to you. Talk through your risks with somebody you know and get good advice from somebody who knows.

PEOPLE ISSUES

People issues include the broad range of social and psychological factors that have a great influence on the decisions we make. These can be more influential (often unknowingly) on your decision-making than the need to be profitable.

Some of the social factors involved in our decision-making are personal attributes like competitiveness or compassion, our attitude to risk and growth, or the desire to be liked by our friends and neighbours. There are also strong social ties that complicate decision-making including connections to the family, community and the land.

Dealing with complexity requires a higher level of people skills and an ability to assess the many options available. It helps to get advice, work with others collaboratively and/or improve your own level of knowledge, when making a complex decision.

If you are thinking of employing people in a small business, it is nearly like taking somebody into your family. Think carefully about the attributes and attitudes you expect from your employees.

Your customers are people. If you do not like dealing with people, do not choose a business that relies on dealing with them, e.g. a restaurant.

GETTING GOOD INFORMATION

When we don't rationally consider risk, simple or complicated decisions can become complex. This is because unnecessary uncertainty is involved.

You can avoid or reduce uncertainty and unwanted risks through thorough analysis – gathering the available information, synthesising and analysing, talking it through is a process of good decision-making. You can also use your intuition and experience to deal with some of the uncertain elements of a decision if you know you can trust your instinct.

TOO MUCH OR NOT ENOUGH INFORMATION?

The amount of information you need changes with experience; the challenge is to determine at which point further analysis will not reduce uncertainty – some uncertainty always remains.

PULLING IT ALL TOGETHER

Photo: A. Renkin



Decisions are never made based on isolated pieces of information – rather they consider the whole system incorporating personal, financial and environmental aspects.

Considering how the different components of your farming system interact can be useful in understanding the impacts of decisions. How would you illustrate your farm in terms of all the different components? Sketch or map your farming system on some butchers paper. Use visual tools like this to better understand the complexity of your farm business decisions.

Some people are highly skilled at putting all of the parts of the process together.

Intuition or using instinct is also important. The reason instinct is useful and appropriate

for complex decisions is because we need to use our experience to take into account many factors at once and come up with the best decision in the circumstances. So, don't be afraid after you have 'put all the pieces together' to listen to your instincts as well.

THE LAST WORD: A CAUTIONARY TALE

A study by INNOVIC¹ has shown that less than 4% of new business ideas are likely to be commercially successful. The main issues were that innovators frequently over-estimate their potential sales and under-estimate the time and costs associated with bringing a new product to market.

The study concluded that good market research, realistic financial projections, a good management team and a strong business plan can greatly improve the chances of success.

Factors that most commonly lead to business failure are listed on the following page to further highlight the importance of managing risks and making good decisions for your business. It is important to note that a combination of these factors contribute to more than half of new business ventures failing.

FACTORS THAT COMMONLY LEAD TO BUSINESS FAILURE:

Business Skills & Experience

- Lack of business experience
- An inadequate business plan, poor overall planning, lack of focus
- Underestimating the skills and knowledge required
- Lack of networks in the industry, poor supply chain knowledge and management
- Wrong choice of industry, product or business model
- Bad business location:
 - Neglecting competition or opportunities to cooperate
 - Poor judgment of site suitability, water, soil and climatic conditions.
 - Accessibility/logistics
 - Infrastructure, resources and services
 - Labour

Personal skills, goals and expectations

- Confusing a business with a hobby or retirement activity
- Unrealistic expectations, e.g. following fads and fashions
- Entrepreneurial over-enthusiasm and burnout
- Poor time management, procrastination - wrong timing and poor coordination of farm management activities and/or business management and marketing activities.
- Poor ability to recognise opportunities and/or foresight and flexibility to adapt to changing conditions and technologies.

Understanding the market

- Focus on field production and neglect of market realities
- Underestimating distance to markets and associated costs
- Underestimating the competition from other regions or other products
- Trying to be fast on the market with a new product that has not been properly developed or cannot be supplied in the required volumes

and losing potential customers due to poor service or lack of supply (getting a bad name)

- Putting all eggs in one basket – e.g. just one product or one big client or one investor.

Financial management

- Poor capital structure - too much debt
- Financial overspending:
 - No adequate budget and funds for establishment costs
 - Poor cash flow management
 - Taking on additional, non-budgeted overheads or costs to grow the business faster
- Lack of reserve funds - failing to prepare for volatile markets and uncontrollable cost increases e.g. for water and energy, materials and equipment, production inputs (fertilisers, sprays), and labour costs, natural disasters, management mistakes etc.
- Poor internal controls - accounting, staff management, customer service etc.
- Employee incompetence (bad staff selection, supervision, no training, no job descriptions).
- Poor record keeping and analysis of records (financial and production) or failure to act on analysis results (ignoring the 'plan – do – review' imperative).

Communication

- Ineffective marketing and promotion – poor communication skills.
- Poor customer service resulting in lack of repeat business (not listening to what customers² say, working on assumptions about the market and individual customer requirements).

1. INNOVIC is a not for profit organisation assisting innovators, helping to turn new ideas, inventions and innovations into viable products and new businesses. See: innovic.com.au

2. Your customer is the person or business you are dealing with directly, which is often not the final customer of your product.

FURTHER INFORMATION

Enterprise Connect: www.enterpriseconnect.gov.au

Business Tasmania: www.business.tas.gov.au

Business Mentor Services Tasmania: www.mentors.org.au

Tasmanian Small Business Mentor Service: www.coachestuff.com

Local Business Enterprise Centres: <http://www.becaustalia.org.au/>

The Huon Sirolli Network: www.huonsirolli.org or contact Lesley Kirby the Huon Sirolli Enterprise Facilitator on 0438 503 528 lesley@huonsirolli.org

SPROUT: <http://www.sprout.org.au/>

Please contact your local council for information on local producer groups in your area.

For more information please refer to NRM South's Healthy Farming & Environment Reference Guide: <http://www.nrmsouth.org.au/>