GREENHOUSE GROWER

2018 STATE OF THE INDUSTRY

Uncertainty on the Regulatory Front Means It's Time to Get Involved

With election dynamics, a new farm bill, and pending immigration reform in the mix, 2018 looks to be a wait-and-see year for the horticulture industry.

By Craig Regelbrugge

A new year is upon us, and so it's time to peek at what the coming months may bring from an advocacy perspective. The task gets tougher as our politics seem to get more dysfunctional and defy prediction. Many factors contribute to this dysfunction — a Congressional redistricting process that has left only a few Congressional seats truly competitive for either party; a hyperactive 24-hour news cycle coupled with the reality that many Americans get their news from a source that tells it like they want to hear it; and an erosion of trust and confidence in anchor institutions including government.

After year one, is the Trump administration winning or losing? From purely a business perspective, it's a mixed bag. On one hand, there have been areas of (mostly regulatory) relief, and some President Obama-era labor, environmental, and other initiatives have been or are being rolled back. The stock market keeps charging along, unemployment is low, and consumer confidence is high. On the other hand, investors and businesses tend to prefer certainty. Yet certainty seems in short supply. Where may we be headed?

Big Legislation in 2018?

Many Washington observers believe that Republicans squandered their opportunities during the first half (or more) of 2017. So as the year wound down, Senate and House Republican leaders doubled down to get major tax relief and reform bills across the finish line by Christmas. As of our press deadline, it was too early to call the outcome, but we looked to be in a good place on preserving cash accounting, and soon we'll know whether the Senate and House can move bills and resolve their differences.

2018 is a mid-term election year, with the whole House of Representatives and one-third of the Senate up for grabs. Election dynamics are going to make it tough to move major bills, yet what might be possible?

Cows, Sows, Plows … and Horticulture

The next Farm Bill is scheduled to be written in 2018. With rural America a central focus for politicians of both parties, many will want to get a bill done, and farm bills offer significant opportunity for bipartisan cooperation.

For horticulture, the Farm Bill is now a major vehicle for funding research and innovation, and for addressing plant pests and diseases that threaten business performance and growth.

19% Suppliers who say government regulation is one of the issues their companies are currently facing.

Source: *Greenhouse Grower*'s 2018 State of the Industry Survey

With Farm Bill support, AmericanHort is leading efforts to modernize greenhouse and nursery plant certification and safe trade. Our top priority will be to preserve and strengthen a handful of key Farm Bill programs that advance our industry.

On the topic of certification, our pilot program with USDA for offshore-produced vegetative cuttings got into full swing in December. Participating growing operations in six Latin American countries have implemented a risk-reducing systems approach, and imports are being monitored through March 31. More than one billion vegetative cuttings are imported each year to be grown on in the U.S. If the pilot is effective, it will enable expedited entry of these highly perishable starter plants, a sort of Global Entry for a key part of our supply chain.

Will 2018 See Relief From Growing Labor Woes?

A top industry concern continues to be the labor force, with most employers saying they have more job openings than applicants. Employers are using many strategies to deal with the worsening labor crisis — strategic investments in mechanization and automation, alternative labor sources such as refugees, or entering into programs like H-2A. Yet, there's no complete substitute for an immigration reform bill that stabilizes horticulture's current workforce and provides better legal programs for the future.

Unfortunately, the politics around this issue are a mess. When 14 farmers, including Tom Demaline, the board chairperson of AmericanHort, sat with President Trump and Agriculture Secretary Perdue in late April, they left convinced that real progress is within reach. However, key presidential advisors and political appointees in departments like Justice, Labor, and Homeland Security are unsympathetic or downright hostile.

"Regardless of how you feel about politics, decisions made (or deferred) at every level of government will continue to have a huge impact on business, and the business of horticulture. For this reason, opting out of politics and direct, personal involvement in advocacy is not now, and never has been, a sound business strategy." — Craig Regelbrugge

44% Growers who are concerned about governmental regulations.

Source: *Greenhouse Grower*'s 2018 State of the Industry Survey

AmericanHort is Working Hard on Your Behalf

Against this backdrop, AmericanHort is working on three fronts — legislative, administrative, and treaty-based. On the legislative front, it is not difficult to outline a solution that provides a reliable visa program for future workers, a way for experienced but unauthorized current workers to get right with the law and earn legal status, and integrity to the employment eligibility verification process.

For now, the hard-liners are uninterested in compromise, and all eyes are on whether and how Congress will address the fate of some 800,000 young people brought to the U.S. as children who have received relief from the threat of deportation. The so-called DACA (Deferred Action for Childhood Arrivals) issue has a hard deadline of March 5, after which status will begin to expire, so it will be the test of whether a sensible compromise can be reached.

On the administrative front, we worked with the National Council of Agricultural Employers to develop a menu of policy and regulatory changes that would make the H-2A visa program more workable. If we can gain some ground on administrative reforms, it will mean some relief for current and prospective H-2A users.

Finally, with the ongoing North American Free Trade Agreement (NAFTA) negotiations, we are exploring treaty-based opportunities for better agricultural worker exchange between the U.S. and Mexico. The NAFTA process itself is quite uncertain, but our intent is to leave no stone unturned.

Transportation

Getting plants to the market relies heavily on a functioning transportation system. In mid-December, new requirements took effect regarding drivers' hours of service and electronic logging devices (ELD). We've spoken with a number of growers who ship on their own truck fleets and felt they were well prepared for the changes. Yet, most growers expressed great concern about trucking in terms of cost, availability, and drivers. Driverless trucks soon? Until then, we will be monitoring compliance and enforcement in this area, as well as any renewed efforts to drive investment in renewing America's aging infrastructure.

Regardless of how you feel about politics, decisions made (or deferred) at every level of government will continue to have a huge impact on business, and the business of horticulture. For this reason, opting out of politics and direct, personal involvement in advocacy is not now, and never has been, a sound business strategy. The future will belong to those who perform now, grow tomorrow, and prepare. AmericanHort wishes you all the best for success together in 2018! GG

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Dealing With Your Banks in 2018 Will Take Patience

Financial institutions are still reluctant to part with capital for agricultural and horticultural growth, despite economic indicators. Here's why banks have raised the bar on lending.

By Barry Sturdivant

Almost every day the Dow and NASDAQ are hitting all-time highs. Unemployment is low and housing starts continue to be vibrant — all good news for nursery and greenhouse growers. These trends are expected to continue for the next couple of years. With the wind at the economy's back, commercial and agricultural lending should be at an all-time high. But it's not. What's going on?

Banks Are Not Inclined to Gamble on Horticulture

After the 2016 election, bank stocks soared with the anticipation of an improving economy and the prospect for lighter regulation. A year later, bank stocks are growing at only half the rate of the S&P 500. The growth rate for business loans is at the lowest level since the first quarter of 2011. At Wells Fargo, total loans actually fell by 1%. This is surprising given the low unemployment rate, gross domestic product growth of 3.3%, and a rise in private business investment.

"For the foreseeable future, expect your bankers to be tight on the front end when you are requesting funds for expansion of inventory or facilities ... Grow slowly and carefully into your market." — Barry Sturdivant

Banks suffered losses in the Great Recession from 2008 through 2011. The hangover of the recession wasn't worth the party of the growth years that led up to it. Lenders have not forgotten. Interest rates have remained low for more than a decade, which means banks are unable to charge a meaningful spread over their cost of funds to compensate for potential loan losses. Add to that the higher reserve requirements resulting from Dodd-Frank, and banks have become even more risk-averse than usual. They aren't making many business loans, and they really aren't interested in making loans to agricultural producers.

Bankers See Manufacturing Companies as a Safer Bet

It is a view that is shaped by years of consolidation, shrinking profit margins, growers' lack of preparation for the down cycles in the economy and, in some cases, it is the result of poor management practices.

These issues are not just peculiar to the green industry, they have affected agriculture more profoundly than the economy in general. As a result, many of the bankers who still refer to themselves as agricultural lenders have shifted their focus to food manufacturing and distribution, commonly known as FMD in ag lending circles.

FMD is characterized by companies that are taking raw agricultural products and making finished food items out of them. In other words, banks want to finance potato chip makers, but they don't want to finance potato growers; former ag lenders are calling on companies that make pancake mixes, but they probably won't call on the wheat farmers, and so on.

FMD companies have no production risk, and this is something that is attractive to those banks still trying to pretend they are involved in agricultural lending.

Greenhouse and Nursery Operations Are High-Risk Ventures

Banks perceive both greenhouse and nursery operations to have higher risk profiles. Let's admit it, they're right. Greenhouses remained profitable during the Great Recession, but profit margins have shrunk.

Greenhouses are, of course, specialized facilities, which banks don't like to finance. Not that long ago, the return on investment for most new greenhouse construction was five years. That was in the days of better profit margins and before price increases in steel, glass, and concrete, not to mention increases in minimum wages and health care.

Banks are now balking at the longer payback time for new greenhouses, and don't really care if they have a useful economic life of up to 50 years. They focus on greenhouses that have sold for less than market values under distressed circumstances, while conveniently forgetting it was their brilliant idea to put the property up for auction during the winter. It's hard to get many interested bidders when it's too late to produce a spring crop.

As for nurseries, inventory builds took place from 2000 through 2008 like the party was never going to end. Most were left unprepared for the housing slump. They were over-produced on inventory and slow to react. Many tried to hang onto their inventory while it kept absorbing cash for its upkeep. They couldn't wait out the recession.

Lenders were complicit in the over-production during the growth years. They were fat, dumb, and happy looking at their borrowing base certificates, showing they were well collateralized with inventory. Most still haven't figured out their mistake in trying to shoehorn nurseries into asset-based, meaning collateral-based, lending structures. They don't want to try to understand the working capital and cash flow requirements and have, instead, mostly abandoned lending to these operations.

> 39% of growers who took *Greenhouse Grower's* 2018 State of the Industry survey indicated they're concerned about the economy.

> "Financing is important to help during the slow season. It's industry specific, as we need the money to build inventory and pay employees when little revenue is coming in. Sometimes its hard to find someone who understands our industry."
> – Grower response from 2018 State of the Industry Survey

What You Can Do to Prepare

All agricultural production presents a higher risk for lenders. What complicates matters for the green industry is that you don't grow a commodity. A farmer can produce a mountain of grain and an ocean of milk and it still is sold. It may occasionally sell for below breakeven, but there is cash returning to the farm and that can buy some time to make corrections. It's not quite so simple for nurseries and greenhouses. A large amount of overproduction isn't sold at any price.

For the foreseeable future, expect your bankers to be tight on the front end when you are requesting funds for expansion of inventory or facilities, and expect them to be impatient and possibly irrational if you should run into trouble. Grow slowly and carefully into your market. Leverage your long-term lending capacity to make sure you have a cash cushion. Building up long cycling nursery inventory is similar to buying a piece of equipment and, likewise, should be largely financed with current cash flow. Growing nursery inventory on a borrowing-base certificate that only considers the collateral value is a ticking time bomb for everyone.

More and more, the lending void being left by larger money center and regional banks backing away from production agriculture is being filled by community banks and non-bank banks. In many cases, they are supported by Farmer Mac and other funding sources at competitive rates, terms, and conditions. They are looking for credit worthiness in their borrowers, but it is good to know lenders still exist to support and promote production agriculture. **GG**

Barry Sturdivant (barry.sturdivant@tsagfinance.com) originates loans for TS Ag Finance. You can contact him via email or at 951-541-4004.

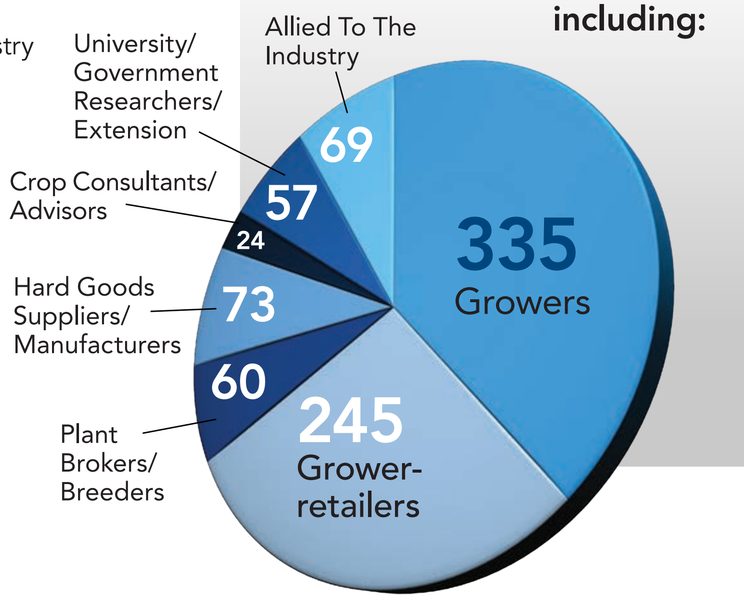
The Outlook For '18 Is Positive, Survey Says

Greenhouse Grower surveyed growers, grower-retailers, researchers, and suppliers for the 2018 State of the Industry report, to learn about industry trends, challenges, opportunities, and concerns. Here's an overview of what to expect this year.

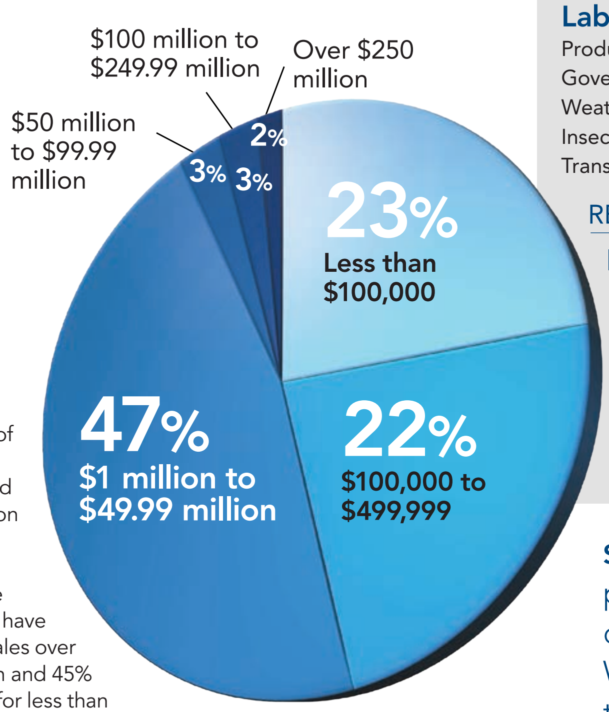
By Laura Drotleff
Editor | ldrotleff@meistermedia.com

With the U.S. economy doing well and growers experiencing economic growth, the industry is poised for another good year in 2018, according to *Greenhouse Grower*'s 2018 State of the Industry Survey. This year's report might look a little different to you. Instead of going into every detail of the survey questions, we hit a few highlights and reserved the rest of the analysis for some upcoming articles and web extras. For the full analysis and report, you can download the detailed whitepaper that holds much of this year's survey data on **GreenhouseGrower.com**. GG

Greenhouse Grower's 2018 Survey included 863 Respondents, including:



What is your company's annual sales volume?



Just 8% of growers surpassed $50 million in sales in 2017, but more than half have annual sales over $1 million and 45% account for less than $500k in sales annually.

Top Concerns for 2018:

GROWERS & GROWER RETAILERS:

Labor (61%)
- Production Costs **(54%)**
- Government Regulations **(44%)**
- Weather/Changing Weather Patterns **(42%)**
- Insect & Disease Pressure **(40%)**
- Transportation Costs/Availability **(25%)**

RESEARCHERS:

Insect & Disease Issues (58%)
- Weather/Changing Weather Patterns **(47%)**
- Economy **(45%)**
- Production Costs **(44%)**
- Pollinator Health **(36%)**
- Water **(36%)**

SUPPLIERS:

Competition (63%)
- Grower Consolidation **(33%)**
- Economy **(30%)**
- Labor/Availability of Qualified Workforce **(30%)**
- Weather **(28%)**
- Transportation/Fuel **(27%)**

Weather, labor, the economy, production costs, and transportation availability and costs are concerns across the board, as are ongoing pest and disease issues, and marketing to new consumers.

Supplier Feedback: "The consolidation and professionalization of the industry is a challenge to be sure, but it is a welcome one. We all need to run tighter and quicker ships to stay afloat in this industry, and we welcome the challenge!"

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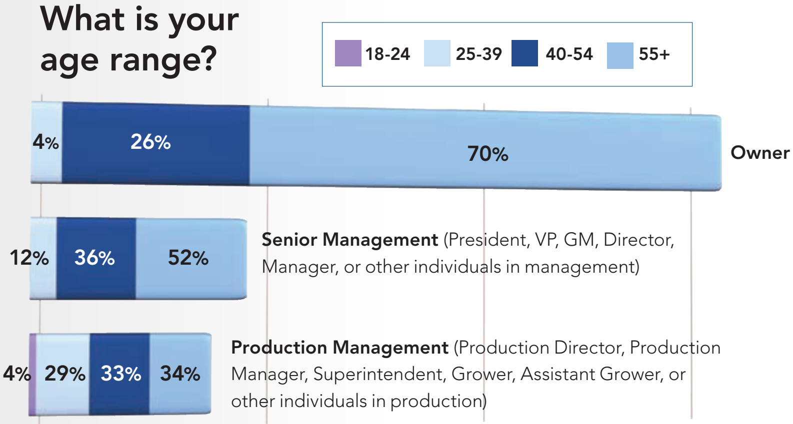
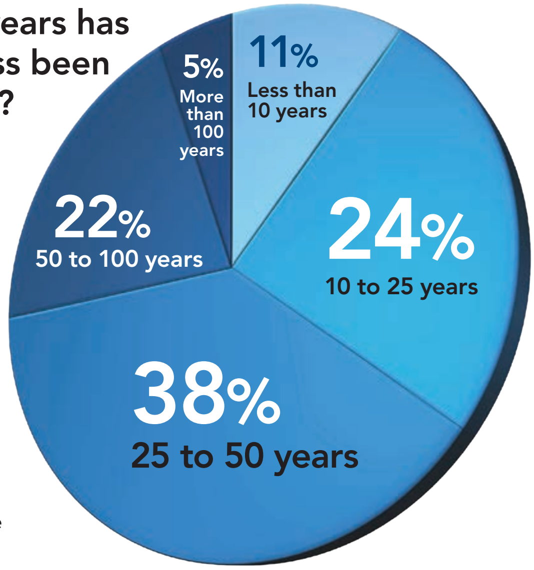
What is your age range?



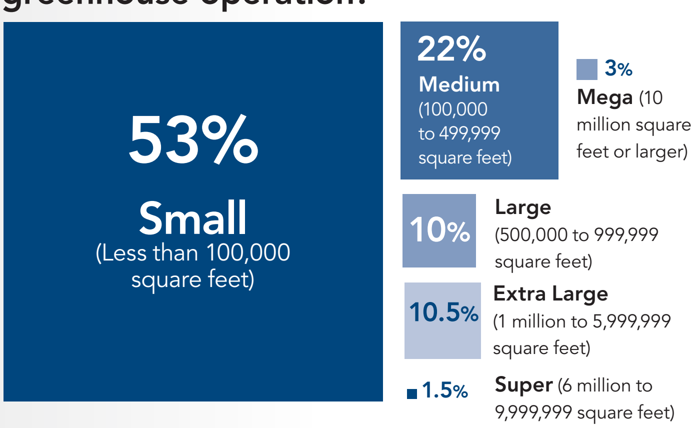
Owners of grower operations are aging, and roughly half said they have a member of the next generation ready to take over when they retire.

How many years has your business been in operation?

There's a shortage of new growing operations in the market, as 65% have been in business for more than 25 years. Meanwhile, there's also a shortage of next generation business people (born after 1970) ready to take over existing greenhouse operations.



What is the size of your greenhouse operation?



Small grower and grower-retailer operations make up the majority of our industry, but this number is down slightly from 57% in 2016.

Which of the following customers do you serve?

Top customers for growers and grower-retailers include direct sales to consumers, other growers, independent garden centers, and landscapers. We expect to see sales to the landscape segment, as well as e-commerce, increase in the coming years.

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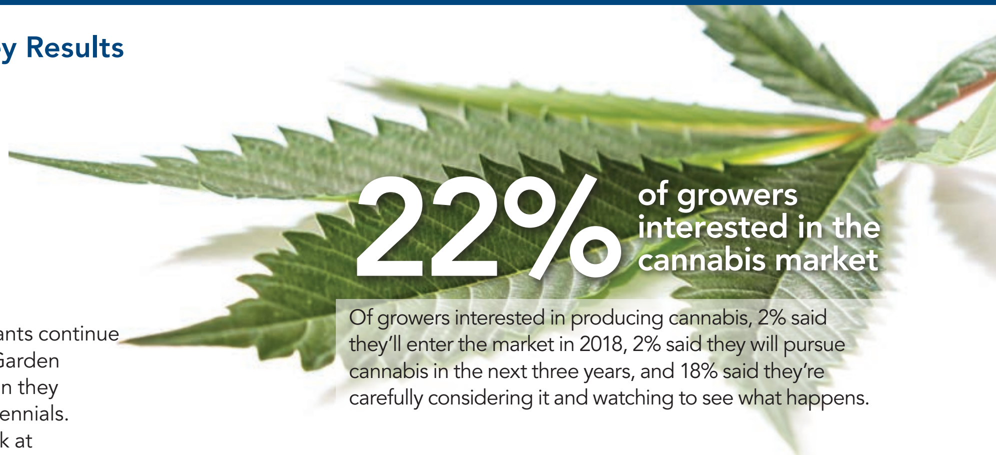
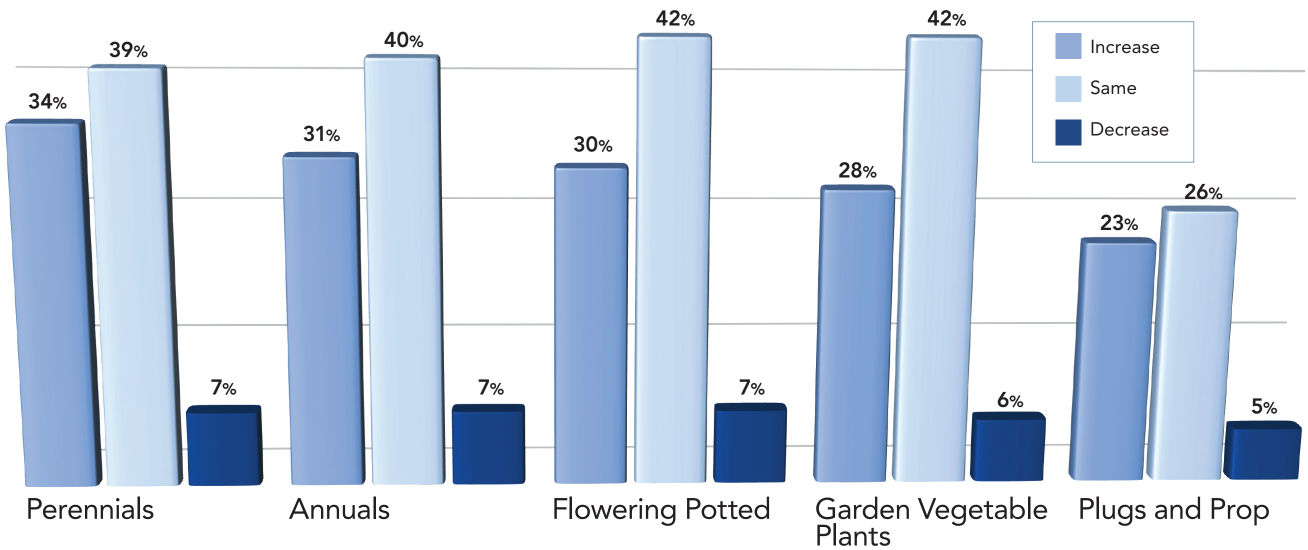


22% of growers interested in the cannabis market

Of growers interested in producing cannabis, 2% said they'll enter the market in 2018, 2% said they will pursue cannabis in the next three years, and 18% said they're carefully considering it and watching to see what happens.

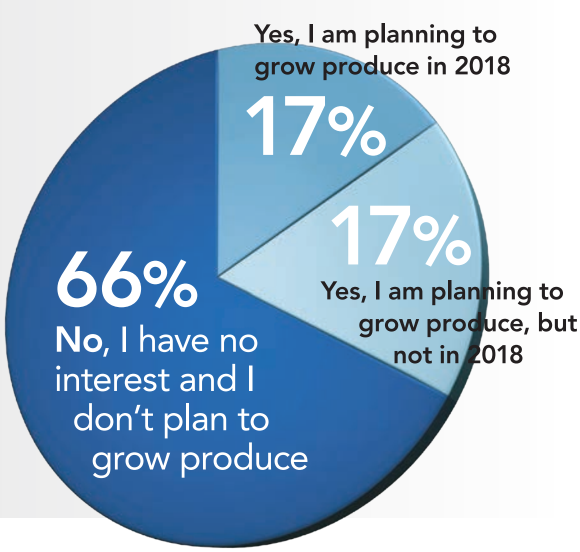
Top Crops in 2018

Perennials, annuals, and flowering potted plants continue to be the largest growth areas for growers. Garden vegetables are down slightly from 2016, when they were the second largest crop (32%) after perennials. Meanwhile, more growers are starting to look at emerging areas like cannabis and hydroponic vegetables.



Do you have any plans to grow produce?

Some growers are filling the gaps in their crop schedules by growing and selling greenhouse produce for the fresh market (i.e. hydroponic produce).



Top 3 crops for growers who produce food crops in greenhouses:

1. **Tomatoes (72%)**
2. Leafy Greens (63%)
3. Peppers (44%)

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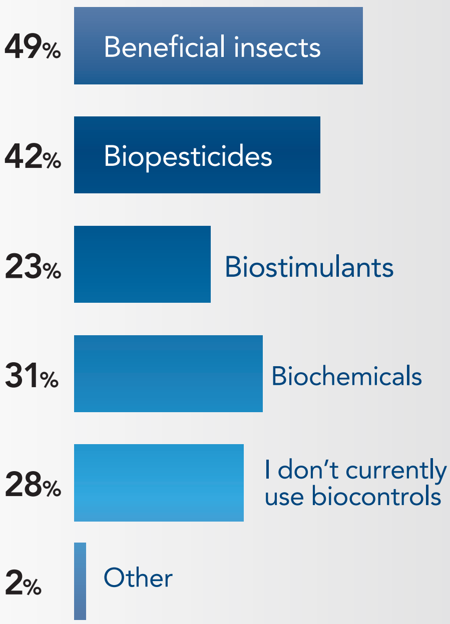
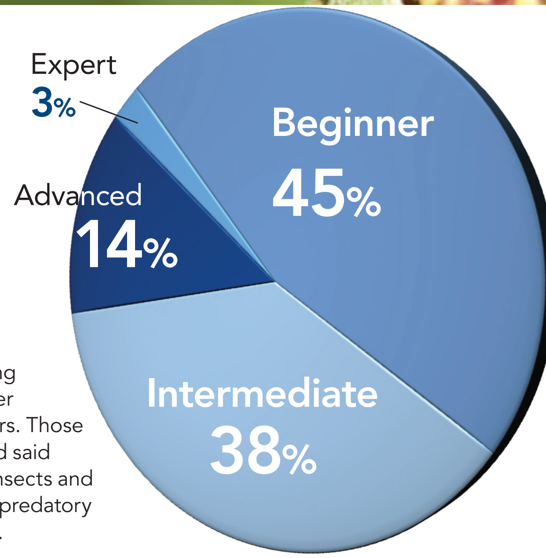
What types of biocontrols do you use?

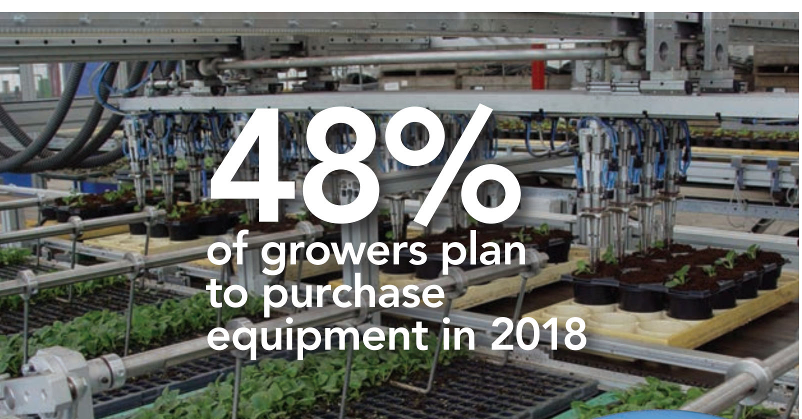
More than half of the growers surveyed are using all types of biological products, and we expect that number will continue to increase with more research and education.



What level of experience do you have with using biological controls?

Nearly half of growers using biological controls consider themselves to be beginners. Those who are more experienced said they are using beneficial insects and biological control agents (predatory insects) and biopesticides.





Top operational goals:

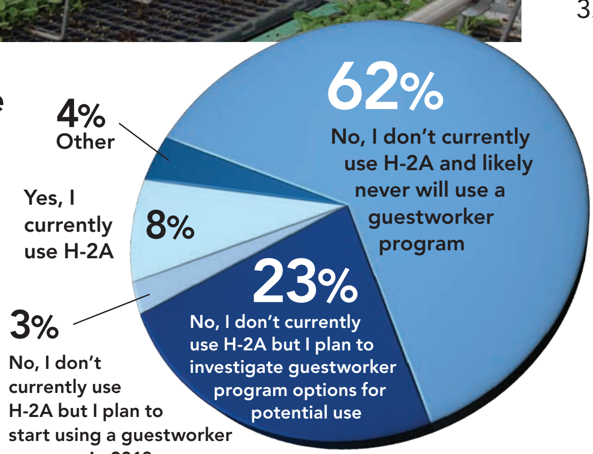
1. **Increase efficiency (70%)**
2. Improve product quality (59%)
3. Increase margins (57%)

Top areas where growers plan to invest in 2018

1. **Greenhouse Structures & Coverings (45%)**
2. Computer Services & Technology (25%)
3. Irrigation Equipment (23%)
4. Soil & Amendment Handling (22%)
5. Planting Equipment (19%)

Do you use the H-2A program?

Growers are starting to look at their options for foreign labor as the availability for domestic labor continues to shrink.



Researcher Challenge: "Know the cost of doing business. This is the key factor in your business plans. No matter what you do in the future, you need to know your bottom line."

71% Researchers are spending more time looking for funding

Grower Concern:

"Going neonic free. It took two to three years of trialing and testing to assure we were ready for it and still produce the quality we expect at a similar cost structure."

Areas that need more dedicated research:

Technology
Biological controls
plant breeding
Consumer research
PEST AND DISEASE management and resistance
lighting

Where does your operation currently stand with neonicotinoids?

49% Do not use neonicotinoids

25% Use neonicotinoids minimally, as necessary, or as a last resort

13% Still use neonicotinoids

6% Are in process of eliminating neonicotinoids from production

3% Are certified organic, and never used neonicotinoids

(4% said this issue is not applicable to their operations)