When prices for land lost its grounding and management accounting was set-aside

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Abstract
This study addresses the current situation in the Danish agricultural sector when prices for land lost its grounding and management accounting was set-aside.
Agenda

- Some background information on the Danish Agricultural sector
- Objective and research questions
- Methodology
- Findings and implications

Some background information

- Historically low profit industry.
- The industry is capital intensive, huge investments in land, buildings and live stock compared to present turnover.
- Asset turnover 0.31 in 1991, 0.09 in 2009, for an average full-time holding. Manufacturing companies in Denmark AT > 1.0
- Easy access to debt financing:
  - Up to 70 percent financing by mortgage banks
  - Nearly the rest financed by banks
  - For young farmers equity often < 0 within the first year
### Some accounting information from an “average” farm holding

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<th>2003</th>
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<th>2006</th>
<th>2007</th>
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<tbody>
<tr>
<td>EBIT from agricultural</td>
<td>573.285</td>
<td>652.464</td>
<td>740.221</td>
<td>986.508</td>
<td>819.150</td>
<td>816.855</td>
<td>403.570</td>
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<tr>
<td>activities</td>
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<td>Profit from agricultural</td>
<td>86.157</td>
<td>168.832</td>
<td>270.801</td>
<td>448.556</td>
<td>110.711</td>
<td>(415.902)</td>
<td>(531.579)</td>
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<td>activities before tax</td>
<td></td>
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<td>Profit from all activities</td>
<td>185.687</td>
<td>332.393</td>
<td>426.925</td>
<td>624.865</td>
<td>293.804</td>
<td>(307.768)</td>
<td>(438.802)</td>
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<td>agricultural assets</td>
<td></td>
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<tbody>
<tr>
<td>Return on agricultural</td>
<td>4.44</td>
<td>4.44</td>
<td>4.69</td>
<td>3.05</td>
<td>2.61</td>
<td>1.20</td>
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<td>assets</td>
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<td>Return on equity</td>
<td>1.75</td>
<td>1.72</td>
<td>1.68</td>
<td>0.59</td>
<td>-0.56</td>
<td>-0.90</td>
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<tr>
<td>Market interest rate a)</td>
<td>3.40</td>
<td>2.99</td>
<td>3.60</td>
<td>4.22</td>
<td>4.14</td>
<td>3.05</td>
<td></td>
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</tbody>
</table>

### Development in real prices

![Graph showing development in real prices for houses and farms](image)
Objective and research questions

- Economic rationale cannot justify the price increases seen on the aggregated level within the agricultural sector.
- An entire sector seems to be in u-topos
- The objective of this paper is to expose causes that have led to the economic bobble in the Danish agricultural sector and left this industry in a huge crisis.
- Research questions:
  - What are the farmers’ motives for engaging in investments that does not generate an economic profit?
  - What role have the agricultural advisors taken during the decision processes that have led to the present situation?
  - Why have financial institutions financed investments in the agricultural sector that is obviously unprofitable?

Methodology

- The study is based on a qualitative case study that includes semi structured interviews with:
  - bank managers and staff in agriculture departments in two banks located in two different areas of Denmark.
  - In one of these areas three farmers were interviewed individually, and in the other area 8 farmers participated in a focus group interview.
  - In each of the two areas one agricultural consultant was also interviewed.
- All interviews was recorded and transcribed for further analysis.
- The data is analysed by using the pragmatic constructivist framework
Facts

- They are extremely focused on the concrete phenomena of their business
- The phenomena are made manageable via non-financial performance measures
- The credit draft account is a central yardstick for financial control.
- Other financial performance measures are not used in the managerial decision process, except for communication with banks.
- The coupling between accounting numbers and concrete phenomena are found too abstract
Values

- Being a farmer is a deep rooted part of their identity and self-perception
- They enjoy showing you their holdings and possessions, but they would never dream of revealing last year’s profit
- They are extreme optimists
- They have a true belief in economies of scale and general increases in efficiency as the way to solve decreasing terms of trade
- What counts is size – to grow is the most important success factor
- They run “cigar-box” financial control if there is an opportunity to grow and it can be financed, then they go for it.

Communication

- Three main groups of actors:
  - Financial institutions
  - Farmer’s association
  - Farm consultants (owned by the farmer’s associations)
- The remaining society is a hindrance – they ask too many questions that are difficult to answer. Relatively low degree of communication
Communication

- Communication with Financial institutions are made via budgets and annual accounts
- Unequal communication, the farmer delivers information, that is often produced by his advisor, and the bank decides for further lending on that basis.
- If the bank says go then the farmers perceives this as a confirmation of the rightness in the decision
- Until 2008 banks never said no → growth was beyond dispute
- Such practice was by the farmers perceived as an accept and a reward for setting management accounting aside.

Communication

- Agricultural advisors work are employed by the farmers via the farmers’ association.
- As a result of structural changes, the advisors has become profit centres.
- The single farmer is now the customer who should be given what he asks for – no critical voice.
- The farmers have low trust in the advisors. Therefore the advisors are mainly used for administrative tasks.
Possibilities

- The farmers see growth in volume as the only possibility to develop their business.
- Their main focus on non-performance indicators supports this strategy: more milk per cow, more piglets per sow, etc. (at any price).
- And when possible: more animals, more land, etc. (at any price).
- Since accounting logic is set-aside there is no attention pointed at alternatives.
- Advisors are reduced to clerks.
- The surrounding society is out of reach, they only talk about environmental care and organic farming.

Implications

Facts                 Possibilities
                         
Communication       

Reality

Values
Implications

- Based on this extreme case!
- Non-financial performance measures has one directional attention: more is better or less is better.
  - Good for revenue or cost
  - But no automatic focus on profit.
  - Thereby the actions of actors might harm the overall performance of the company
- The logic of economics and accounting is cost vs. Benefits
  - Automatic balanced focus.
  - But on a more abstract level because actions of actors have been translated into monetary units

Questions and comments