

# Smalltown Businesses Also Caught in Farm Financial Stress

*The effects of the agricultural crisis have also been felt among business operators in small towns of North Dakota. Our recent survey of business operators provides a first-hand glimpse at how farm events affected nonfarm businesses, the management adjustments operators made, and their expectations for the next few years. Businesses that started up in the 1970's appear to have been hurt most by declining revenue and falling equity in the farm sector. Business operators were nonetheless cautiously optimistic about the future.*

Tough times on the farm translated into tough times for business operators in many parts of smalltown America. They were caught in the same financial pressures as farmers.

We came to those conclusions after examining trends in retail sales, net cash farm income, and cash receipts from farm marketings in North Dakota. Our survey of business operators in six representative towns in North Dakota confirmed what the trends showed. (See box, "About the Survey.")

North Dakota was experiencing a substantial recession at the time we conducted the survey. Taxable retail sales, adjusted for inflation, declined nearly 17 percent statewide during 1980-86 (table 1) and receded to levels of the early 1970's. Not all counties have declined equally. Total retail sales declined 28 percent for agricultural counties from 1980-86, but only 14 percent for nonagricultural counties. Thus, not only has the retail sales pie been shrinking, but ag-dependent

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## Why North Dakota?

North Dakota has the highest percentage of agriculturally related counties in the Nation. Almost three-fourths of its counties are agriculturally dependent. Agriculture, in fact, accounted for 44 percent of North Dakota's economic base in 1985. Agriculturally dependent counties are those in which farming contributed a weighted annual average of 20 percent or more to total labor and proprietor income from 1975-79.

counties were losing their share of that shrinking pie.

Trends in net farm income and farm cash receipts were remarkably similar to those for retail sales (fig. 1). Retail sales peaked slightly later than net farm income, but have followed the same downward trend since the late 1970's. All three have returned to levels of the early 1970's.

The decline in retail sales in ag-dependent counties is reflected in employment patterns except that the percentage changes are smaller. From 1980-86, employment declined by 1 percent in agricultural coun-

ties but increased about 10 percent in nonagricultural counties and about 6 percent statewide.

## Community Effects

We asked the business operators we surveyed how the farm crisis had affected their community. Effects on the business community were the most frequently mentioned. Many reported closing of businesses and loss of business volume, indicating that an average of almost seven businesses had closed and three had opened in the last 2 years. The types of businesses most frequently mentioned as having closed were clothing stores, hardware stores, and machinery and implement dealers. Eating places and clothing stores were most often mentioned as having opened. When we compared their perceptions to what had actually occurred in their towns, we found that the operators had slightly underestimated the number of openings and closings, but had accurately identified the types of businesses affected.

Respondents also commented on the types of businesses that would be most and least affected if the economic stress in farming were to continue for 2 more years. Nearly 40 percent of the business operators indicated that farm machinery dealers would be most affected, while about 15 percent said that all types of businesses would suffer. Nearly half identified grocery stores as being least affected.

## Financial Characteristics

Selected 1985 financial characteristics of the businesses surveyed are summarized

**Table 1—North Dakota's ag counties trailing far behind others in retail sales and employment**

County type	Counties	Total retail sales			Total employment			
		1980	1986	Change	1980	1986	Change in employment	
		Number	Million dollars	Percent	Number	Number	Percent	Percent <sup>1</sup>
Agricultural <sup>2</sup>	39	825	596	-27.75	109,643	108,558	-1,085	-0.99
Other	14	2,761	2,384	-13.65	203,392	223,197	+19,805	+9.74
All	53	3,587	2,980	-16.92	313,035	331,753	+18,718	+5.98

Constant 1986 dollars.

<sup>1</sup>(1986 value minus 1980 value) divided by 1980 value.

<sup>2</sup>As defined by Bender et al. 1985.

Source: North Dakota Job Service, 1980, 1986.

in table 2. While the median net profit was \$13,000, 21 percent reported a loss and another 22 percent reported less than \$10,000 net profit. Losses were generally associated with high debt levels. Only 79 percent of those with more than 70-percent debt were current on their debt repayments compared with 93 percent of those with less than 40-percent debt. About a third of these businesses had no debt, yet nearly a fifth had debt/asset ratios exceeding 70 percent. The average debt/asset ratio was 39 percent, and about 37 percent of the businesses had ratios of 40 percent or higher. The businesses surveyed did not appear to have an excessive debt load compared with similar businesses nationwide. However, the data concerning net profit suggest that many of these firms may have difficulty servicing their debt under current conditions.

### Adjusting to Hard Times

How are businesses adjusting to lower sales and delinquent accounts? The most frequently reported adjustments were to increase collection efforts on overdue accounts, reduce inventories, reduce workforce, and charge interest on overdue accounts (fig. 2).

Some types of businesses initiated specific adjustments more often than other types. For example, 79 percent of

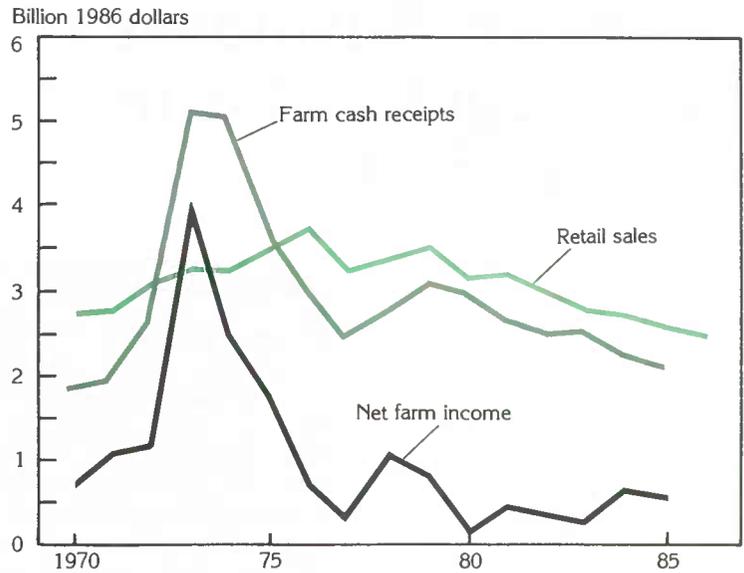
**Table 2—Financial characteristics of North Dakota businesses, 1985**

Item	Amount (median)
Business debt/asset ratio (average)	39.0%
	Dollars
Total assets	126,483
Total debt	21,000
Net worth	75,000
Gross income	116,831
Gross profit	66,302
Net profit	13,000

Median net worth is not equal to median assets minus median debt because some respondents reported their assets but not their debt or vice versa and were thus excluded from the net worth calculation.

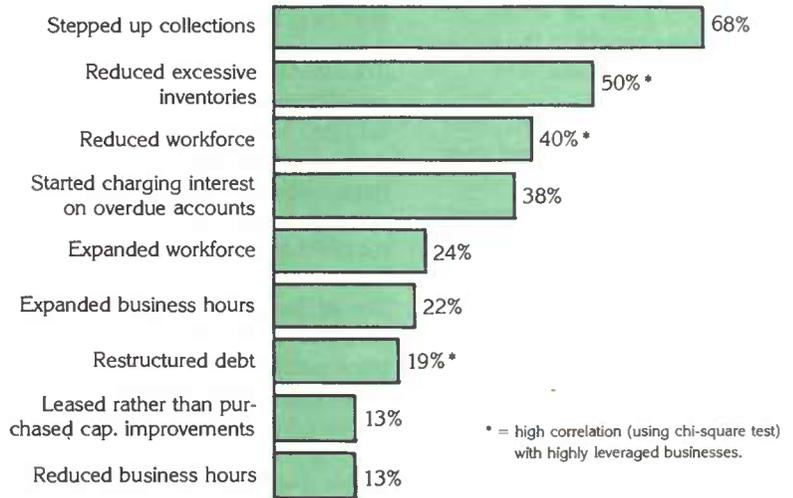
We show only median figures to offset the effect on the mean by a few large companies. For example, the average value of assets was over \$1 million, but the median was a little over \$125,000.

**Figure 1  
North Dakota retail sales mirror decline in farm cash receipts**



Source: North Dakota Tax Department and USDA's Economic Research Service.

**Figure 2  
Management response to slow sales in North Dakota, 1982-85**



retail firms and 67 percent of wholesale durable goods firms reported that they had reduced their inventories. Construction and nondurable manufacturing firms were most likely to have reduced their payrolls. But not all firms were cutting back on employees: 45 percent of finance, insurance, and real estate firms had expanded their workforce as had over 33 percent of professional services firms. Wholesalers and firms that manufactured nondurable goods were more likely to charge interest on overdue accounts. Adjustments such as restructuring debt,

reducing inventories, and reducing the workforce were generally undertaken by firms with high levels of debt.

### What's Ahead?

How optimistic are North Dakota's business operators in the face of these challenging economic times? Their responses to several questions about future sales and expansion seem cautious but positive. About 38 percent of the respondents had made major capital

## About the Survey

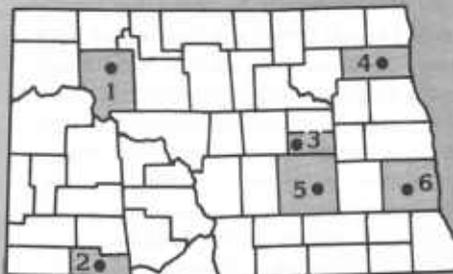
We received more than 600 responses to our survey of current and former business operators in six small communities that are agricultural trade centers: Carrington, Casselton, Grafton, Hettinger, Jamestown, and Stanley (see map). The survey was personally delivered to all local businesses in the five smaller towns and to half of the businesses in Jamestown during the period March-July 1986. Overall, 48 percent of the businesses responded. The towns range in population from about 1,700-16,000.

Survey questions covered finances, trade patterns of customers, inventory acquisition, number of employees, management practices, business outlook for expansion and continuation, and the effects of the farm crisis on businesses and on the community.

The six communities studied are all in heavily agricultural areas, and four are in counties that had a fourth or more of their labor force directly employed in agriculture in 1980. Several indicators suggest that the economies of the six communities have been hurt by the farm crisis. Retail sales, measured in constant 1986 dollars, declined in all six communities between 1980 and 1986, and total employment dropped in two counties the towns were in.

The link between retail sales and the farm sector is revealed in the survey responses. Slightly more than 40 percent of respondents' sales were made to farm families. The percentage of sales accounted for by farmers was smallest in Jamestown, the largest community studied. Nevertheless, the sum of sales to farmers and to local residents accounted for a relatively constant share (about three-fourths) of total sales in each town. Some business operators reported that more than half of their sales went to farmers.

## North Dakota communities surveyed



1	4
<b>STANLEY</b> Pop.: 1,718 % change in retail sales: '70-'86 -36% '80-'86 -36%	<b>GRAFTON</b> Pop.: 5,435 % change in retail sales: '70-'86 -1% '80-'86 -12%
<b>MOUNTRAIL COUNTY</b> Agr. 26% Services 24% Retail 17%	<b>WALSH COUNTY</b> Services 28% Agr. 26% Retail 18%
2	5
<b>HETTINGER</b> Pop.: 1,765 % change in retail sales: '70-'86 -29% '80-'86 -16%	<b>JAMESTOWN</b> Pop.: 16,118 % change in retail sales: '70-'86 +2% '80-'86 -16%
<b>ADAMS COUNTY</b> Agr. 28% Services 25% Retail 16%	<b>STUTSMAN COUNTY</b> Services 34% Retail 17% Agr. 13%
3	6
<b>CARRINGTON</b> Pop.: 2,544 % change in retail sales: '70-'86 -36% '80-'86 -37%	<b>CASSELTON</b> Pop.: 1,714 % change in retail sales: '70-'86 -27% '80-'86 -37%
<b>FOSTER COUNTY</b> Agr. 25% Services 24% Retail 19%	<b>CASS COUNTY</b> Services 35% Retail 19% Agr. 5%

Note: Percentages under county information represent industry percent of total employment (U.S. Census, 1983). Retail sales changes are in 1986 dollars.

These included wholesalers of nondurable goods (largely grain elevators and farm supply outlets), agricultural service operators (such as chemical applicators), and manufacturers of durable goods (such as equipment).

improvements in the last 3 years, and about 26 percent saw opportunities for expansion or growth (table 3). Operators in Jamestown (the largest community surveyed) tended to be most optimistic: 34 percent expected to grow, compared with only 14 percent of operators in Carrington and 18 percent in Casselton.

More than 40 percent of the proprietors in finance, insurance, real estate, or professional services saw potential for expansion in the next 3 years. In contrast, less than 25 percent of retailers saw such opportunities. Retail operators were also the least optimistic concerning the continuation of their business: about 20 percent did not know whether their business could continue for the next 3 years, and another 9 percent felt continuation was unlikely.

On the positive side, about 60 percent believed their net profit would grow and 62 percent expected their sales or volume

**Table 3—North Dakota business operators' economic outlook, 1986**

Item	Survey response
	Percent
Major capital improvements in past 3 years:	
No	62.1
Yes	37.9
Likelihood of expanding business in next 3 years:	
Very likely	11.9
Likely	14.4
Unlikely	25.8
Very unlikely	24.8
Do not know	23.1
Likelihood of continuing to operate business for next 3 years:	
Very likely	56.3
Likely	22.0
Unlikely	2.8
Very unlikely	2.5
Do not know	16.5
Expected change in sales or service volume in 1986 vs. 1985:	
-20 percent or less	14.3
0 to -19.9 percent	23.7
1 to 20 percent	50.7
21 percent or greater	11.3
Expected change in net profit in 1986 vs. 1985:	
-20 percent or less	16.7
0 to -19.9 percent	22.1
1 to 20 percent	51.8
21 percent or greater	9.4

of service to increase. About 78 percent believed they could continue in business for at least the next 3 years, about 5 percent believed they could not, and 17 percent did not know.

## Implications

Our results indicate that the business community of North Dakota's smalltown agricultural trade centers was affected considerably by the slumping farm economy. Very little research on rural smalltown businesses has been undertaken, but we believe these findings to be typical of rural small towns in similar sparsely populated areas of the Plains States. Our data may serve as a benchmark for additional studies on the interrelationships between the farm economy and rural smalltown businesses.

Coping with the challenges posed by a declining economic base will require both individual action by business operators and collective efforts by local business and community groups. Individual measures that some businesses may use to try to

stem their losses include improved inventory control, firmer management of accounts receivable, and more effective use of personnel. In fact, the survey results reveal that many businesses have been taking such measures. In addition, many smalltown businesses could benefit from advertising and promotion designed to take advantage of a small store's strengths, such as superior service, convenience, and awareness of customers' special needs. Such firms may also be able to take advantage of buying groups or resident buying offices to reduce the cost of goods sold, and some vendors may be willing to assist in advertising and promotional efforts.

Collective efforts by business or community groups typically fall into two categories: (1) efforts to capture a larger share of local (or tourist) trade and (2) efforts to expand the area's economic base. The first category includes promotional campaigns (sometimes involving special entertainment events), measures by business associations to coordinate hours and improve the physical attractiveness of the business

district, and efforts to recruit new or replacement businesses to "round out" the local trade and service sector. The second category typically includes attempts to attract new basic employers, to retain or expand existing firms, and to encourage local entrepreneurs to establish new enterprises.

While all of those strategies are appropriate for a community to pursue, many observers believe that efforts aimed at encouraging establishment and expansion of local firms deserve greater attention. Especially in economically depressed rural areas, programs aimed at assisting communities retain their existing businesses may require approaches that emphasize community-wide involvement as well as assistance to individual entrepreneurs. Since operators undergoing financial difficulty do not differ substantially from those experiencing less difficulty, programs aimed at addressing the economic and social environment of the community, as well as improving the skills of individual business managers, may be necessary. **RDP**

### Former Business Operators

Who better can describe the effects of dwindling retail sales than operators who have gone out of business in these six towns? We compared the characteristics of the former business operators who responded to the survey with those of the current business operators and former farmers. Our sample was small (68 former business operators), but the survey did yield some interesting results.

Current and former business operators reported similar reasons for establishing their businesses. When we compared the types of businesses, we found that most of those that had gone out of business were retail establishments. Fewer professional services firms and those in the finance, insurance, and real estate category had gone out of business. Former business operators had been involved in their business for a much shorter period than those

still operating, and their businesses were comparatively new. There was little difference in the types of customers they served: 40 percent of their customers were farmers.

The dominant pattern is that the businesses that failed were similar to, but smaller and less well-established than, other firms in the study communities. Because most of these failed businesses were started in the 1970's, the effect of economic stress in agriculture on business operators may have been similar to its effects on farmers and ranchers. Business operators who established their firms in the 1970's, like those who began farming during that period, appear to have been severely affected by declining revenue and falling equity. Circumstances, rather than individual actions, may thus have been the major cause of failure for many rural businesses.

### For Additional Reading . . .

Lloyd D. Bender, Bernal L. Green, Thomas F. Hady, John A. Kuehn, Marlys K. Nelson, Leon B. Perkinson, and Peggy J. Ross, *The Diverse Social and Economic Structure of Nonmetropolitan America*, RDRR-49, U.S. Department of Agriculture, Economic Research Service, September 1985.

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