Extension Service
West Virginia University

How To Avoid Losing Your Shirt In Aquaculture

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Back in 1981, I was invited to a party for investors in a shrimp farm, Aloha Technology, Inc. (that's not the real name), that was starting in Hawaii. The guests were greatly enjoying the shrimp that were piled on the table.

I approached one rather distinguished-looking gentleman who looked like he might be a business executive, and engaged him in conversation about the venture.

Had he known the officers of the corporation long?
No, only a few weeks.

Did he know much about their background?
No, nothing really, He thought Dr. Jones, who was putting the venture together (I've changed his real name), might have some background in biology.

What did he think of the site?
Never saw it.

Which method of raising shrimp was going to be used?
Didn't know.

Which species of shrimp was going to be grown?
Wasn't sure.

How about the market for shrimp?
Thought it was pretty strong.

How much had he invested?
$100,000.

Why?
He liked the taste of shrimp

A few years later, the Aloha Technology was in bankruptcy; Dr. Jones had left the state; the landlord was looking for a new tenant; and my friend, who liked the taste of shrimp, had lost his $100,000.

Sound familiar? In my 15 years with the Hawaii State Aquaculture Program, I've seen a lot of failures-- some by Fortune 500 companies, with millions of dollars, and some by much smaller concerns, with just a few investors. These failures have involved a wide range of plants and animals, raised in many different culture systems. Interestingly and importantly, they have much in common.

By bringing the common threads of failure to your attention, I home to save the industry further embarrassment and, hopefully, save you, the prospective investor, your hard-earned money.

Here are ten recommendations:

1. Don't invest in aquaculture just because you like the taste of the product.

Investing in a shrimp or lobster farm obviously has more "sex appeal" than say investing in ball bearings. My warning: you may not be able to eat ball bearings, but you might make a lot more money there. I've got nothing against your taking an interest in your investment, but it may be a lot cheaper in the long run to buy your favorite seafood rather than farming it. The best kind of investor is one who brings some kind of worthwhile experience to the table, in addition to money.

2. **Thoroughly investigate the people who are after your money.**
   He's tall, blue-eyed, well-spoken, wears an expensive business suit ..might even have a Ph.D., and he is trying to get you to invest in his company. Be careful. I can't say that every attractive person is a con man, but I can tell you that I've seen very few con men who weren't attractive! Before giving anyone a dollar, take them apart, with special attention to their reputation and credit history. Ask yourself questions, like:
   A. How much aquaculture experience has this fellow had? Has he ever managed or worked on a farm?
   B. Now much business experience has he had? Is he an academic type who has never entered the "real -world" of meeting a payroll? *Perhaps the single most important reason why aquaculture farms have failed in Hawaii has been the lack of business expertise.*
   C. Is he promising a quick payoff? Even the best investments won't yield a penny for several years.

3. **Visit your local state or county aquaculture office for assistance.**

The fact that you, as a potential investor in an aquaculture venture, are reading this now is something of a minor miracle. Amazingly, over the years, of the hundreds of investors in Hawaii's aquaculture industry, only a handful have ever contacted our ADP office, which is one of the most active in the country. It's quite astonishing when someone shows up with a question like: "Who is this Dr. Jones and do you really think he can produce 30,000 pounds of shrimp in a one acre dirt pond in a month?" Yes, chances are we know Dr. Jones and his reputation (good or bad), and be able to provide you with a vast amount of information on culture methods, marketing, permits, disease prevention, etc. In short, we would be able to tell you if the venture has a good shot at succeeding.

4. **Determine the market for the proposed product.**

A few days ago, I received a call from a gentleman on the Mainland who had been developing an aquacultured product at considerable expense over the last six months. I asked him how much market research he'd done.. He told me that he thought the market was good, but he'd made no phone calls. Nor had he ever visited the area where his product would be sold. In addition, he was unfamiliar with the trade journals and what little information he did have, was more than a year old. Not surprisingly, he did not know what to charge.

Of course, he was putting the cart before the horse and inviting a business disaster. What do the principals in the proposed venture know about marketing their product? Whether one is selling a fish or a shoe, one must determine the quantity of saleable product (now and in the future): where it will be sold, to whom, in what form (fresh, live or frozen, for example), and the price that is likely to be received. One might also ask if the venture is planning to "push the market" to expand sales.

5. **The venture must start off "lean and mean."**

Every successful aquaculture farm I've seen has gone through a period of struggle where the principals have lived in modest dwellings, driven older vehicles, and eaten a lot of beans. Keeping costs low is absolutely essential in a beginning venture.

An immediate tip-off as to the future success of the operation is the amount of money the officers plan to pay themselves. Salaries in the $20,000 to $30,000 range are fine, although I would like to see lower than that. Aloha Technology, Inc. had a payroll of close to $600,000 for a dozen workers, who worked less than 10 acres of dirt ponds. One farm was paying its chairman over $300,000 a year to preside over an operation that was so small, you could have thrown a rock across their ponds! (Fortunately, he is no longer there and the farm is now profitable).

6. **Carefully check the accuracy of the business plan**.

Of course, I am assuming there is a business plan. There are two areas where the principals are likely to fudge: expected price and expected production. In my experience these very seldom prove to be accurate.

One can expect a degree of optimism, but it is important to know when optimism gives way to wildly hopeful expectations and just plain lying. One individual I know told potential investors that his product would bring $90 a pound, when reality *was* more like $10 a pound. And I have seen "business plan production" quadruple the accepted industry norm. The problem is everyone knows the price of a Big Mac, but nobody knows how much you have to pay for a snail, a red abalone, or a ghost shrimp. Better check with your local aquaculture office.

Another tip: check to see what the business plan says about security precautions. Proper security on a farm is crucial to the success of the operation. One pass of a net on a dark night could bring the business to its knees, but this important consideration is rarely mentioned to investors.

7. Determine whether the site is suitable for the product.

In aquaculture, there are basically two site situations: 1. the principals have been working a site for some other purpose, a dairy farm, let's say, and now want to get into aquaculture; or 2. the principals have decided what they want to raise and have located a site for the purpose of aquaculture. In most cases, number 2 is better; choose a product from the standpoint of market, culture method, disease tolerance, etc., and then undergo an intensive search for the best possible place to raise that product.

I've seen too many cases of attempting to "shoehorn" a critter on to land that was not at all amenable to the growing of that critter. To offer one example, a leading agriculture firm tried to raise freshwater prawns on a large tract of available land close to a mountain. The market for prawns was strong, the price was high, and the technical help was there in abundance; but after digging 100 acres of ponds, the company realized that the area was too rainy and cold, and the venture suffered a spectacular failure.

8. Choose an expansion operation over a "start-up" operation.

Bankers know that funding a start-up venture is a highly risky proposition. That's why they like to offer loans for expansion purposes.

One piece of advice I've dunned into the heads of entrepreneurs visiting our office has been: "Start small, prove yourself and then build up! " Start with your bathtub or your backyard, if you have to, but put something together that shows you know your technology and equipment; that you have a suitable location that you have actually a marketed product; and above all, that you are willing to learn to walk before you try to run.

I know of countless cases where the principals have leaped into ventures without a pilot-scale operation. To me, this is insanity. I believe 90% *of* the aquaculture investors in this country could have saved the major share of their dollars if they had insisted on a test operation preceding the "full blast" farm.

What scale is desirable? As small as possible to give you an idea of the success of the planned full-scale size. If I had to put a number on it, I would say no larger than 1/10th the size of the proposed fully expanded operation. For how long? A year would be the absolute minimum. Better two years or three.

9. Choose a diversified operation,

Many of Hawaii's aquaculture farmers are now raising more than one plant or animal. By so doing, they are greatly reducing their risk and making better use of their resources. If the market for tilapia takes a dive, you've always got the catfish. Besides, the two might be able to eat the same feed, and you can bring both animals to the wholesaler in the same truck. The most successful farmers I've seen are flexible, always looking out for new opportunities-fast on their feet, with the ability to raise what the consumer wants at short notice. They have a "bread and butter" product, but they also have one that brings in additional income, and yet another they are "fooling around with."

10. Beware of secrecy.

He pulls you to one side and lowers his voice: "This is the cutting-edge. We've got a leg up on the competition. Don't share this information with anyone!"

Wow! Technical breakthrough? Latest stuff? To me, it's a danger signal. Be careful of an attitude that indicates the construction of a fortress. Sure, there can be a great amount of innovation involved in a project and some secrets maybe kept, but aquaculture is still at the stage where--believe me-every ounce of assistance is needed, and unless you are willing to be open with your technology, you’re not going to get any help with your problems.

The way to success in aquaculture is through openness and cooperation. Hawaii's best farmers hold nothing back. They are always eager to see an extension agent and host a tour. I've found that those people who don't allow people on the inside don't know what is happening on the outside, and from a business standpoint, that can be a fatal mistake.

If there's a "secret" in aquaculture, everyone knows it; you make money by dint of your hard work, cleverness and ability to learn from others, paying particular attention to their mistakes and trying not to repeat them.

An Investment Fantasy

So, in light of the above points, allow me to present you with an investment fantasy. One day, a young man named "Bob" comes into my office. He looks strong and energetic, and has some dirt under his nails. I learn that Bob always wanted to do something associated with water and the out-of-doors, and after careful research, decided that farming freshwater prawns was a great idea. He has a degree in biology, but he's also taken a variety of business courses at the University and community college. These have emphasized marketing and accounting. He's even had some sales experience from part-time jobs. After working as an assistant manager of a prawn farm for several years, Bob's decided to start his own farm and has secured 50 acres with a good, long-term lease. He's been working 5 acres of the parcel for the past two years with his own savings, and has shown solid annual production of 2,500 pounds per acre, he's sold his prawns at above market prices, because he's provided his customers with exceptional service. Bob also raises catfish and tilapia, and has made a nice income from these. Bob lives in a small house at his farm, so he can keep an eye on things. He drives an old Toyota, and hasn't been off the island in a few years.

After a lengthy conversation, I discover Bob is well acquainted with the trade journals; has visited our office many times, knows the State extension people well; knows where to get feed and equipment at the best prices; and is not afraid of working 12 hours a day, seven days a week. In fact, he doesn't mind the long hours because he loves what he's doing and plans to be a farmer the rest of his life.

Bob shows me his business plan. He'd like to expand to 10 acres next year, and then bring the farm up to 25 acres in 5 years-if all goes well. He's already got a commitment from the State for a loan with a low rate of interest, but he needs a bit more capital to meet his operating costs. And he'd like to obtain that capital from someone with a good knowledge of seafood marketing to complement his production abilities.

Bob Invites me to see his farm. After he leaves, I make a few phone calls and find out that he gets high marks from other farmers, extension agents, his suppliers (yes, he always pays them on time), and his customers.

The next day, Rob calls and asks if I know any investors.

Would you be one of them?
