

GROWNG FOR TOMORROW

Business Basics for Beginning Farmers



FARM CREDIT EAST

Chris Laughton, Farm Credit East



Agenda

- Introduction
- Recordkeeping
- Financial Statements
- Cash Flow Budgeting
- Financing and Credit
- Q&A

About Farm Credit East

- Part of the national Farm Credit System
- Farmer-Owned Cooperative
- Serving 14,000 customers across seven states
- \$7+ billion invested in Northeast farming, fishing, and forestry
- 100+ year commitment to agriculture
- Programs for Young, Beginning, Small and Veteran farmers



Farm Credit East and our services

- 20 branch offices throughout the region
- 470 dedicated agricultural specialists



GROW  NG FOR TOMORROW

 FARM CREDIT EAST

Define Success for YOU!

- Success is about more than financial gain.
- Your enterprise may have a number of non-financial goals...
- ...BUT, profitability is a pre-requisite to achieving other, non-financial goals.

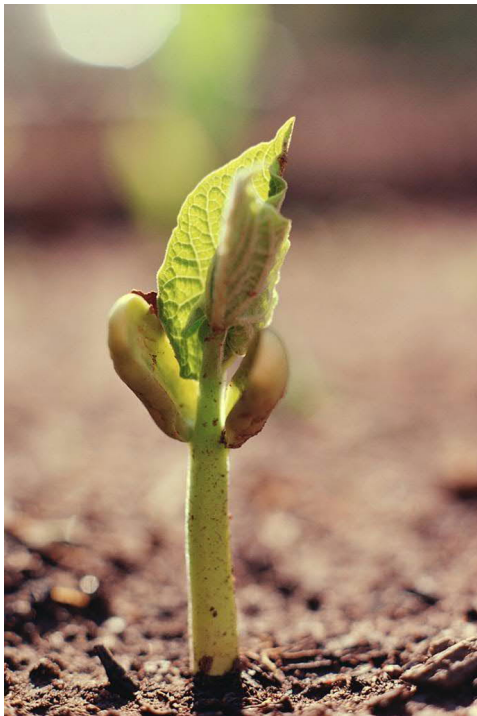


Business Skills

- There are three basic areas of business skills:
 1. Production
 2. Marketing
 3. Financial
- Few people are great at all three. If you are lucky you have two of these skills. Partner or hire the skill(s) you don't have.



Recordkeeping



To run a successful farming operation, you need:

- Labor
- Plants, Crops, or Animals
- Other inputs and supplies
- Land and Equipment
- Good Records!

Plan for Success

- Record keeping is required for taxes – but it can do so much more
- Ultimate goal is to manage from records
- Need up-to-date and accurate records
- Create budget with expectations and measurable results – then compare actual performance to budget—then act!

Farm managers must also be CFOs

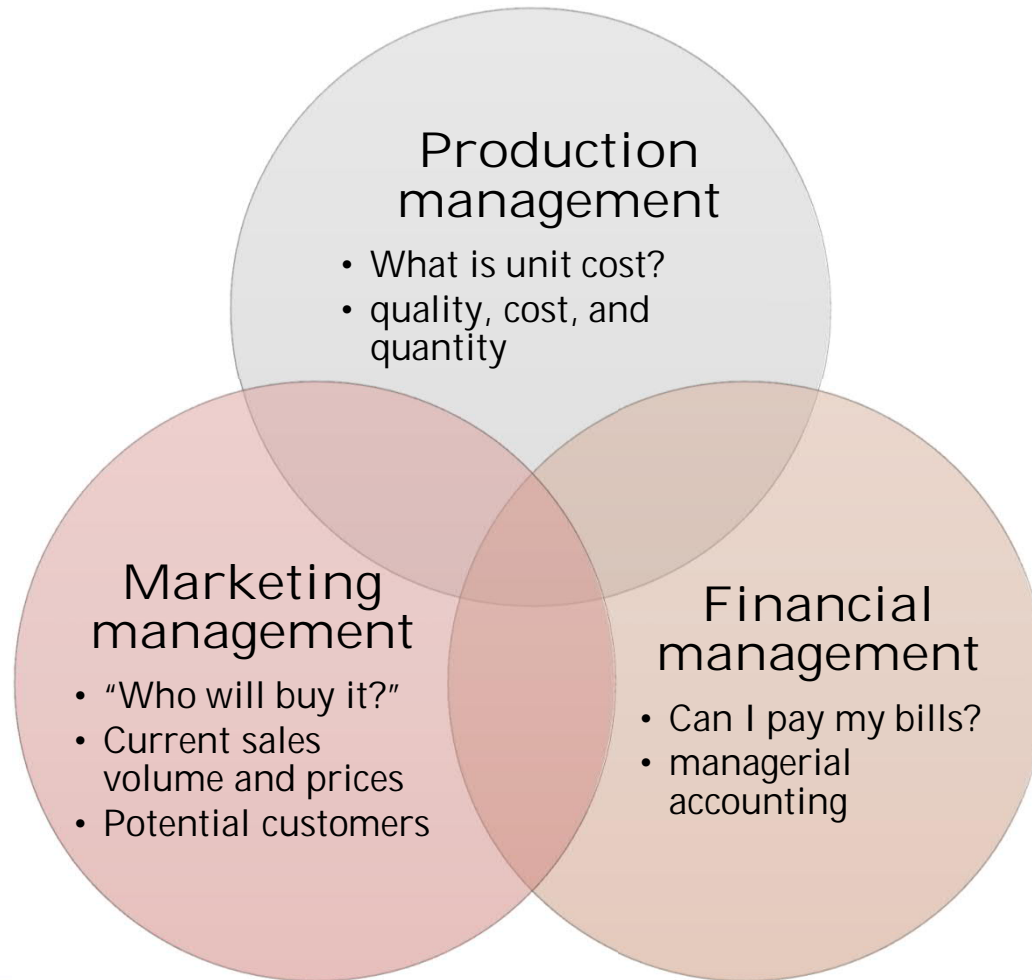
CFO or chief financial officer

The person responsible for:

- financial analysis and planning
- managing assets efficiently
- arranging financing for the business.



Management is key to profitability



The 5-Line Income Statement

Income Statement (for a whole year)	Dollars	% of Sales
Gross Sales or total sales, or income	\$134,400	100%
<u>- Cost of Goods Sold or variable costs</u>	<u>\$80,096</u>	<u>60%</u>
= Gross Margin	\$54,304	40%
<u>- Overhead Costs or fixed costs</u>	<u>\$40,345</u>	<u>30%</u>
= Net Margin or net profit, or profit	\$13,959	10%

Note: In this example, owner draw (pay for the owner) is included in overhead.

Why Cost of Goods Sold (COGS) is important

Another name for cost of goods sold is **variable costs** – the direct costs of producing your product!

COGS = any expense that helps produce one more unit of output

- Production labor
- Seed
- Fertilizer
- Feed
- Fuel
- Supplies

Fixed Costs are Your Overhead Expenses

Another name for fixed costs is **overhead** – the indirect costs of doing business!

These are costs that generally remain the same regardless of variations in your productivity

Examples:

- Office staff & supplies
- Property taxes
- Insurance
- Depreciation
- Anything not directly related to your production

The DIRT-5 of Overhead Costs

- | | | |
|----------|--------------|--|
| D | DEPRECIATION | • Depreciation is the cost of the item spread out over its useful life |
| I | INTEREST | • Interest is the cost of financing the item |
| R | REPAIRS | • Repairs are the anticipated maintenance costs of the item |
| T | TAXES | • Taxes could be property taxes, excise taxes, etc. |
| I | INSURANCE | • Insurance is the cost of insuring the item |

The 5-Line Income Statement, again

Income Statement (for a whole year)	Dollars	% of Sales
Gross Sales or total sales, or income	\$134,400	100%
- <u>Cost of Goods Sold</u> or variable costs	<u>\$80,096</u>	<u>60%</u>
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Note: In this example, owner draw is included in overhead.

Reasons for Low Gross Margin

- Pricing is too low
- COGS is too high
- Shrink is too high

Shrink is any product grown or made (or purchased) but not able to be sold, due to:

- Lack of demand
- Poor quality
- Spoilage
- Theft
- Or other factors...



Fixed Costs or Overhead



Fixed costs do not change with each unit of production. If fixed costs are high:

- Are you too small-scale to be economical?
- Have you “grown into” full capacity?
- Did you overbuild?
- Fixed costs are less manageable after they are implemented.

Accounting Methods



Two different accounting methods may yield different results:

- **Cash accounting:** expenses and income are recorded when money is paid out or received.
- **Accrual accounting:** income and expenses are recorded when earned and incurred, respectively, regardless of when money changes hands.

Accounting Methods

Cash and accrual accounting can yield different results

Cash income:	
Sales of produce - Cash	\$400
A/R payment	<u>50</u>
Total cash income	450
Cash expenses:	
Paychecks Issued	\$300
Gas	20
Supplies	30
Loan payment	40
Total cash expenses	<u>390</u>
Net cash income	\$60

Accrual income:	
Sales – Cash	\$400
Sales – On account	200
Total accrual income	600
Accrual expenses:	
Labor – Accrued payroll	\$400
Gas	20
Supplies	30
Depreciation	300
Total accrual expenses	<u>750</u>
Net accrual income (loss)	\$(150)

Financial Statements



FARM CREDIT EAST

Financial Statements

The 3 Main Financial Statements

Balance sheet

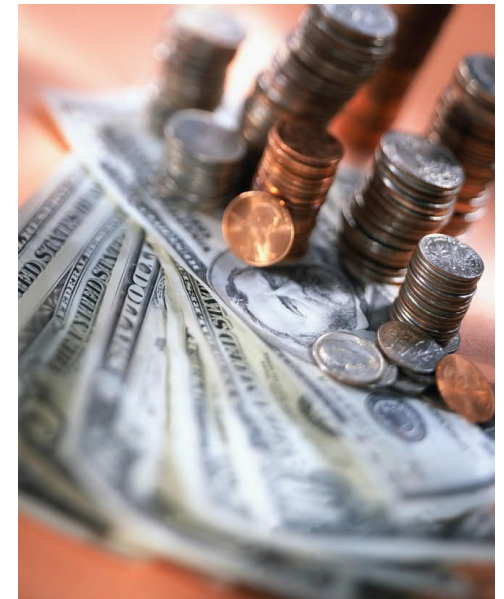
- A snapshot of the business's financial health

Income statement

- Tracks a business's income & expenses over time

Cash flow statement/Budget

- Shows money going in & going out



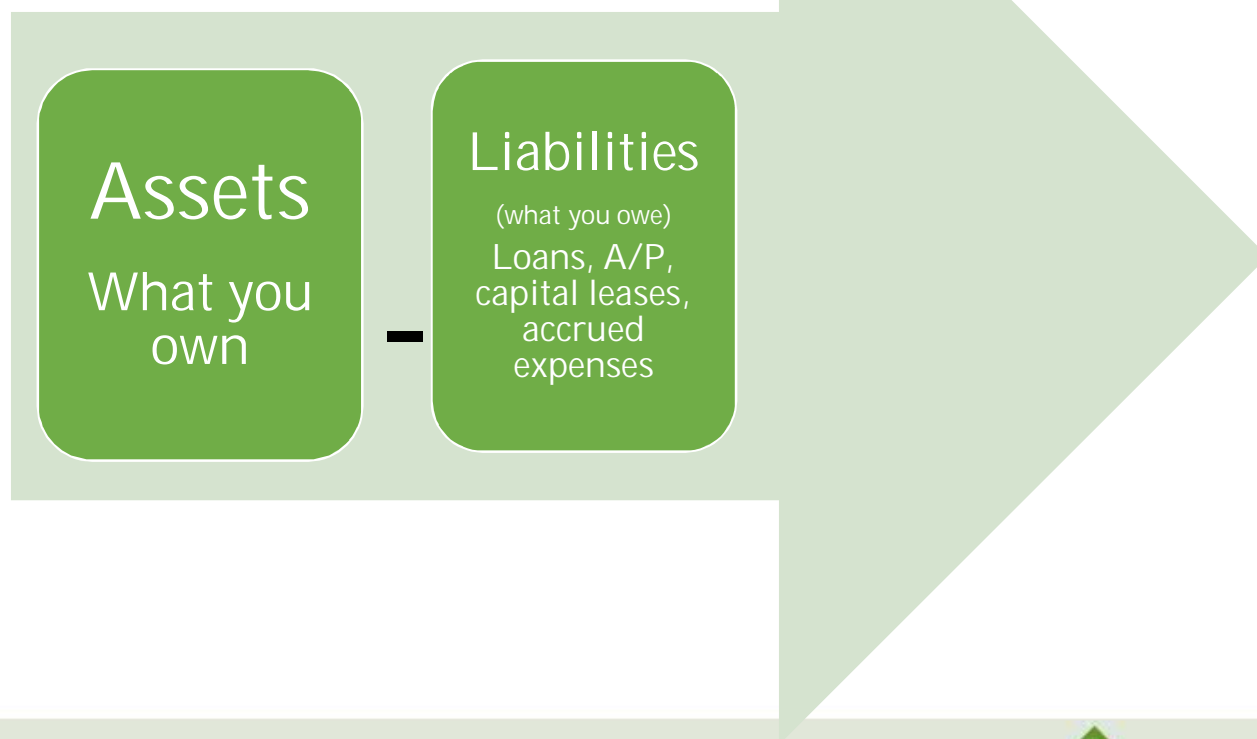
The Balance Sheet

Assets

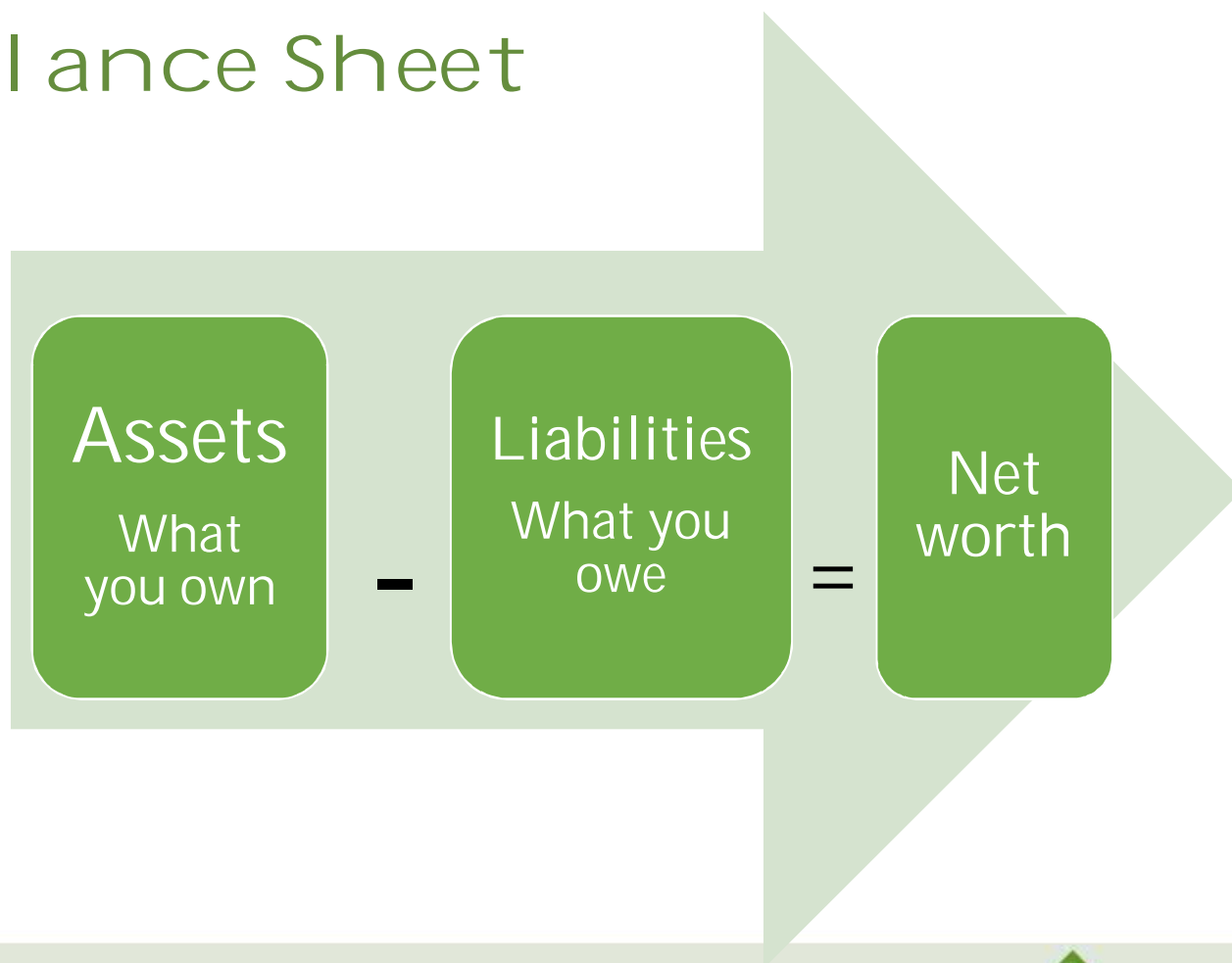
(what you own)

Cash, inventory,
money that customers
owe you (A/R), real
estate, prepaid
expenses, machinery

The Balance Sheet



The Balance Sheet



The Balance Sheet

A Sample Farm Balance Sheet (Dec 31):

Assets		Liabilities	
Checking account	\$11,540	Credit card debt	\$1,000
Supply Inventory	\$1,000	Loan	\$4,500
Equipment	\$4,500	Total Liabilities	\$5,500
Truck	\$10,000		
		Net Worth	\$21,540
Total Assets	\$27,040	Total Liabilities & Net Worth	\$27,040

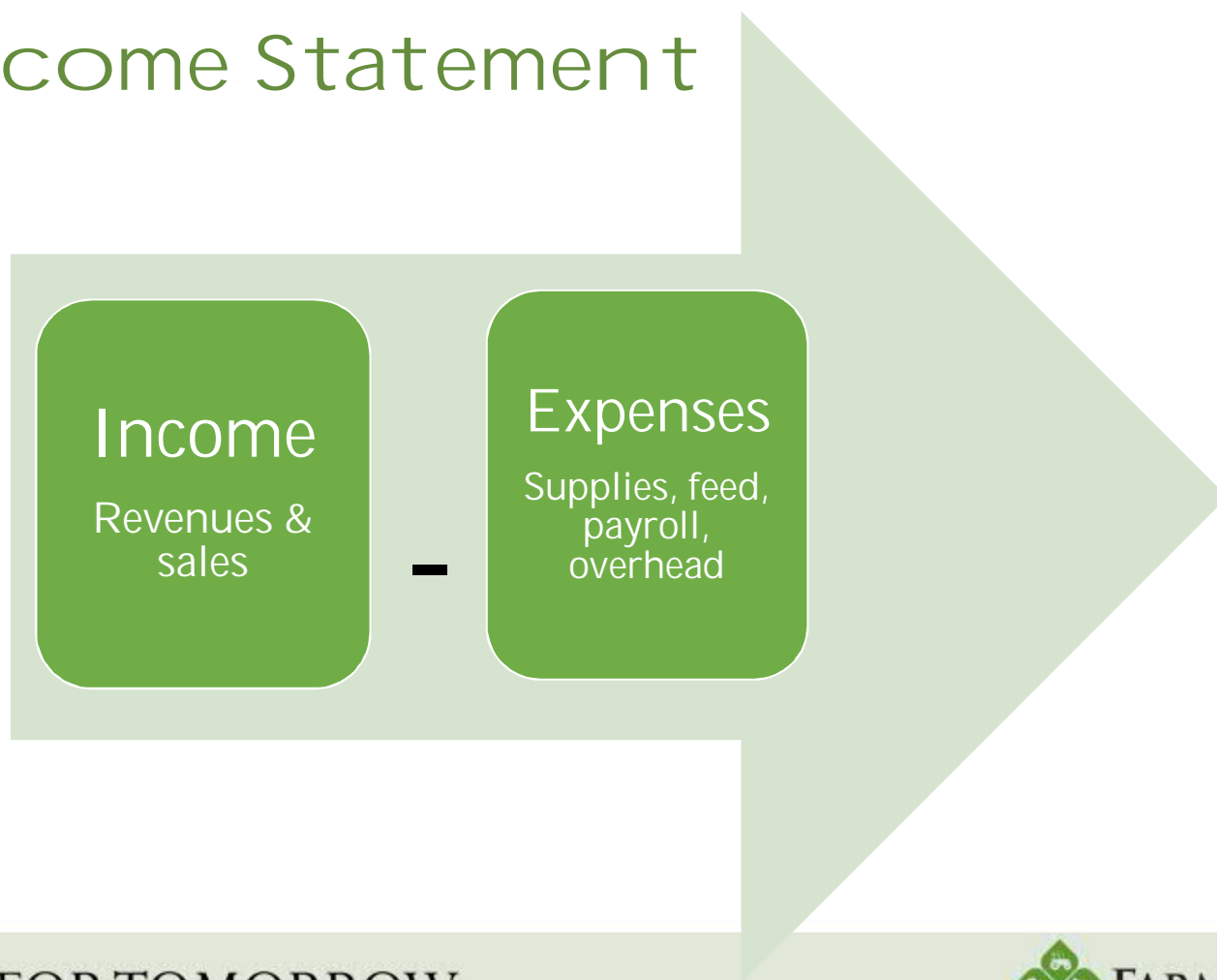
The Income Statement



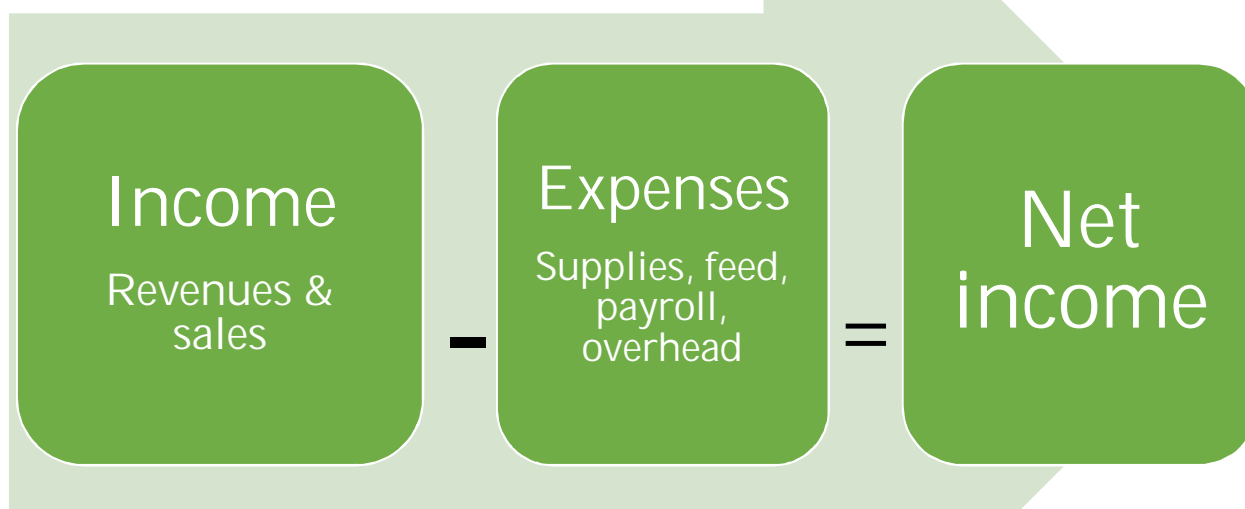
Income

Revenues &
sales

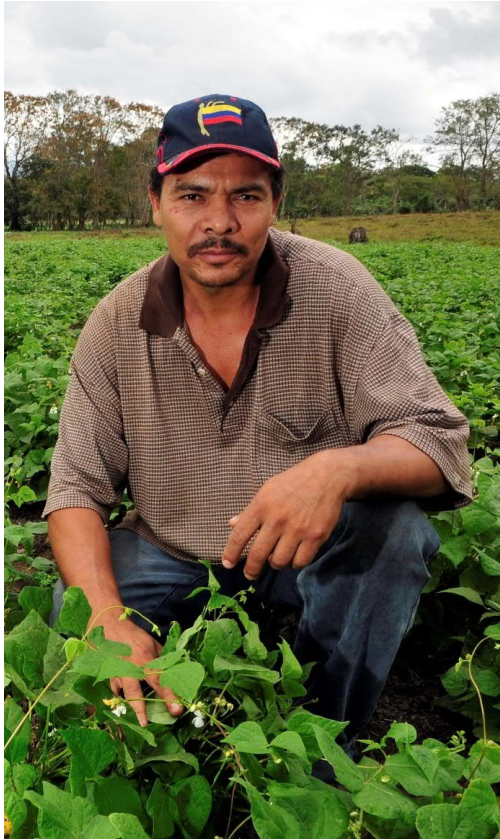
The Income Statement



The Income Statement



The Income Statement (year ending 12/31)



Income:	
CSA Shares	\$61,200
Farmer's Market	64,800
Wholesale Sales	<u>8,400</u>
Total Income	134,400
Expenses:	
COGS	\$80,096
Overhead	10,345
Owner Draw	30,000
Total Expenses	120,441
Net Income (Loss)	\$13,959

Cash Flow Budgeting



FARM CREDIT EAST

Cash Flow Budgeting

JANUARY	FEBRUARY	MARCH
INCOME STREAMS	INCOME STREAMS	INCOME STREAMS
COST OF GOODS SOLD	COST OF GOODS SOLD	COST OF GOODS SOLD
GROSS MARGIN	GROSS MARGIN	GROSS MARGIN
OVERHEAD EXPENSES	OVERHEAD EXPENSES	OVERHEAD EXPENSES
NET PROFIT	NET PROFIT	NET PROFIT
STARTING CASH	STARTING CASH	STARTING CASH
CHANGE IN CASH	CHANGE IN CASH	CHANGE IN CASH
ENDING CASH	ENDING CASH	ENDING CASH

Cash Flow Analysis

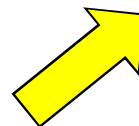
Monthly Results Spreadsheet



Simply Fresh Farm Budget Cash Flow Spreadsheet for Year 2016

	Budget Jan	Budget Feb	Budget Mar	Budget Apr	Budget May	Budget Jun	Budget Jul	Budget Aug	Budget Sep	Budget Oct	Budget Nov	Budget Dec	Budget Annually	% of Sales
Total Income(TI) or Total Sales	10,200	10,200	10,200	5,100	5,100	18,300	16,800	14,400	16,800	14,700	6,300	6,300	134,400	100%
COGS or Total Variable Costs (VC)	-	-	4,038	11,258	7,158	10,506	10,506	10,506	10,506	8,832	6,790	-	80,096	60%
GROSS MARGIN (TI-VC)	10,200	10,200	6,163	(6,158)	(2,058)	7,795	6,295	3,895	6,295	5,869	(490)	6,300	54,304	
GROSS MARGIN %	100%	100%	60%	-121%	-40%	43%	37%	27%	37%	40%	-8%	100%	40%	40%
Total Fixed Costs plus Owner Draw	3,660	4,300	7,275	2,500	2,500	2,570	4,650	2,570	2,570	2,750	2,500	2,500	40,345	30%
NET MARGIN	6,540	5,900	(1,113)	(8,658)	(4,558)	5,225	1,645	1,325	3,725	3,119	(2,990)	3,800	13,959	
NET MARGIN %	64.1%	57.8%	-10.9%	-169.8%	-89.4%	28.5%	9.8%	9.2%	22.2%	21.2%	-47.5%	60.3%	10.4%	10%
Monthly Cash Flow	6,540	5,900	(1,113)	(8,658)	(4,558)	5,225	1,645	1,325	3,725	(1,382)	(2,990)	3,800		
Beginning Cash/Checking Balance	5,000	11,540	17,440	16,328	7,670	3,113	8,337	9,982	11,306	15,031	13,649	10,659		
Ending Cash/Checking Balance	11,540	17,440	16,328	7,670	3,113	8,337	9,982	11,306	15,031	13,649	10,659	14,459		

Cash flows are highlighted in yellow





Simply Fresh Farm Budget Cash Flow Spreadsheet for Year 2016

	Budget Jan	Budget Feb	Budget Mar	Budget Apr	Budget May	Budget Jun	Budget Jul	Budget Aug	Budget Sep	Budget Oct	Budget Nov	Budget Dec	Budget Annually	% of Sales
FARM INCOME														
CSA	10,200	10,200	10,200	5,100	5,100	1,500	-	-	-	6,300	6,300	6,300	61,200	
Farmers Market	-	-	-	-	-	14,400	14,400	14,400	14,400	7,200	-	-	64,800	
Fruit sales	-	-	-	-	-	2,400	2,400	2,400	2,400	1,200	-	-	8,400	
Government Payments	-	-	-	-	-	-	-	-	-	-	-	-	-	
Other	-	-	-	-	-	-	-	-	-	-	-	-	-	
Total Income(TI) or Total Sales	10,200	10,200	10,200	5,100	5,100	18,300	16,800	14,400	16,800	14,700	6,300	6,300	134,400	100%
Cost of Goods Sold (COGS) or Variable Costs														
Production FTE's required	-	-	-	3	3	3	3	3	3	3	-	-	1.75	
Labor- Production	-	-	-	4,800	4,800	4,800	4,800	4,800	4,800	4,800	-	-	33,600	
Labor- Farmers Markets	-	-	-	-	-	1,920	1,920	1,920	1,920	960	-	-	8,640	
Payroll taxes	-	-	-	1,920	1,920	2,688	2,688	2,688	2,688	2,304	-	-	16,896	
Owner's Health Insurance	-	-	-	-	-	-	-	-	-	-	3,200	-	3,200	
Employee Other	-	-	-	-	-	-	-	-	-	-	-	-	-	
Other	-	-	-	-	-	-	-	-	-	-	-	-	-	
Total Labor	-	-	-	6,720	6,720	9,408	9,408	9,408	9,408	8,064	3,200	-	62,336	
Purchases For Resale	-	-	-	500	-	-	-	-	-	-	3,240	-	3,740	
Seed	-	-	3,600	3,600	-	-	-	-	-	-	350	-	7,550	
Fuel	-	-	438	438	438	438	438	438	438	438	-	-	3,500	
Total Crop	-	-	4,038	4,538	438	438	438	438	438	438	3,590	-	14,790	
Transportation	-	-	-	-	-	660	660	660	660	330	-	-	2,970	
Total Farmers Market	-	-	-	-	-	660	660	660	660	330	-	-	2,970	
COGS or Total Variable Costs (VC)	-	-	4,038	11,258	7,158	10,506	10,506	10,506	10,506	8,832	6,790	-	80,096	60%
GROSS MARGIN (TI-VC)	10,200	10,200	6,163	(6,158)	(2,058)	7,795	6,295	3,895	6,295	5,869	(490)	6,300	54,304	
GROSS MARGIN %	100%	100%	60%	-121%	-40%	43%	37%	27%	37%	40%	-8%	100%	40%	40%
Overhead - Fixed Expenses	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	TOTAL	
Vendor Fees	-	-	2,775	-	-	-	-	-	-	-	-	-	2,775	
Insurance	-	1,800	-	-	-	-	-	-	-	180	-	-	1,800	
Interest	-	-	-	-	-	-	-	-	-	-	-	-	-	
Real Estate Taxes	-	-	-	-	-	-	-	-	-	-	-	-	-	
Land Rent	960	-	-	-	-	-	-	-	-	-	-	-	960	
Machinery Rent	-	-	-	-	-	-	-	-	-	-	-	-	-	
Repairs	-	-	2,000	-	-	-	2,080	-	-	-	-	-	4,080	
Utilities	-	-	-	-	-	-	-	-	-	-	-	-	-	
Marketing	200	-	-	-	-	70	70	70	70	70	-	-	550	
Total Fixed Costs (FC) or Overhead	1,160	1,800	4,775	-	-	70	2,150	70	70	250	-	-	10,345	8%
Owner Draw (salary)	2,500	2,500	2,500	2,500	2,500	2,500	2,500	2,500	2,500	2,500	2,500	2,500	30,000	22%
Total Fixed Costs plus Owner Draw	3,660	4,300	7,275	2,500	2,500	2,570	4,650	2,570	2,570	2,750	2,500	2,500	40,345	30%
NET MARGIN	6,540	5,900	(1,113)	(8,658)	(4,558)	5,225	1,645	1,325	3,725	3,119	(2,990)	3,800	13,959	
NET MARGIN %	64.1%	57.8%	-10.9%	-169.8%	-89.4%	28.5%	9.8%	9.2%	22.2%	21.2%	-47.5%	60.3%	10.4%	10%
Other Sources/Uses of Cash														
Equipment purchases	(5,000)	-	-	-	-	-	-	-	-	-	-	-	(5,000)	
Equipment sales	500	-	-	-	-	-	-	-	-	-	-	-	500	
Funds borrowed (loans taken out)	4,500	-	-	-	-	-	-	-	-	-	-	-	4,500	
Funds repaid (loan payments)	-	-	-	-	-	-	-	-	-	(4,500)	-	-	(4,500)	
Net Cash from Other Sources/Uses	-	-	-	-	-	-	-	-	-	(4,500)	-	-	(4,500)	
Monthly Cash Flow	6,540	5,900	(1,113)	(8,658)	(4,558)	5,225	1,645	1,325	3,725	(1,382)	(2,990)	3,800		
Beginning Cash/Checking Balance	5,000	11,540	17,440	16,328	7,670	3,113	8,337	9,982	11,306	15,031	13,649	10,659		
Ending Cash/Checking Balance	11,540	17,440	16,328	7,670	3,113	8,337	9,982	11,306	15,031	13,649	10,659	14,459		

download more info at: www.farmbiztrainer.com/resources/groups/one-page-planning-suite/

GROWING FOR TOMORROW




FARM CREDIT EAST

Top Section:
Farm Income

Next:
Cost of Goods
Sold (COGS)
Itemized by
category

Gross Margin
Calculation

Farm  <small>seed capital</small> Simply Fresh					
	Budget <i>Jan</i>	Budget <i>Feb</i>	Budget <i>Mar</i>	Budget <i>Apr</i>	Budget <i>May</i>
FARM INCOME					
CSA	10,200	10,200	10,200	5,100	5,100
Farmers Market					
Fruit sales	-	-	-	-	-
Government Payments	-	-	-	-	-
Other	-	-	-	-	-
Total Income(TI) or Total Sales	10,200	10,200	10,200	5,100	5,100
Cost of Goods Sold (COGS) or Variable Costs					
Production FTE's required	-	-	-	3	3
Labor- Production	-	-	-	4,800	4,800
Labor- Farmers Markets	-	-	-	-	-
Payroll taxes	-	-	-	1,920	1,920
Owner's Health Insurance	-	-	-	-	-
Employee Other	-	-	-	-	-
Other	-	-	-	-	-
Total Labor	-	-	-	6,720	6,720
Purchases For Resale				500	
Seed	-	-	3,600	3,600	-
Fuel	-	-	438	438	438
Total Crop	-	-	4,038	4,538	438
Transportation					
Total Farmers Market					
COGS or Total Variable Costs (VC)	-	-	4,038	11,258	7,158
GROSS MARGIN (TI-VC)	10,200	10,200	6,163	(6,158)	(2,058)
GROSS MARGIN %	100%	100%	60%	-121%	-40%

Top Section:
Itemized Overhead

Next:
Other Cash Flow
Impacts

Beginning & Ending
Cash Balances

GROSS MARGIN (TI-VC)	10,200	10,200	6,163	(6,158)	(2,058)
GROSS MARGIN %	100%	100%	60%	-121%	-40%
	<i>Jan</i>	<i>Feb</i>	<i>Mar</i>	<i>Apr</i>	<i>May</i>
Overhead - Fixed Expenses					
Vendor Fees			2,775		
Insurance		1,800			
Interest					
Real Estate Taxes	-	-	-	-	-
Land Rent	960				
Machinery Rent	-	-	-	-	-
Repairs	-	-	2,000		
Utilities					
Marketing	200				
Total Fixed Costs (FC) or Overhead	1,160	1,800	4,775	-	-
Owner Draw (salary)	2,500	2,500	2,500	2,500	2,500
NET MARGIN	6,540	5,900	(1,113)	(8,658)	(4,558)
NET MARGIN %	64.1%	57.8%	-10.9%	-169.8%	-89.4%
Other Sources/Uses of Cash					
Equipment purchases	(5,000)				
Equipment sales	500				
Funds borrowed (loans taken out)	4,500	-	-	-	-
Funds repaid (loan payments)					-
Net Cash from Other Sources/Uses	-	-	-	-	-
Monthly Cash Flow	6,540	5,900	(1,113)	(8,658)	(4,558)
Beginning Cash/Checking Balance	5,000	11,540	17,440	16,328	7,670
Ending Cash/Checking Balance	11,540	17,440	16,328	7,670	3,113



Download the live spreadsheet

farmbiztrainer.com/resources/groups/one-page-planning-suite/

Financing Your Business



Equity Financing- Investment

- Start-up or venture capital
- May require you to give up some ownership
- High risk of failure or loss
- Usually comes from self, relatives, angel investor.

Debt Financing – Loans

- Finance ongoing operations or expansion
- Does not dilute ownership – cost is limited to interest
- Often based on collateral
- Banks live here

Investing in the Future

- Invests up to \$75,000 in capital in new & beginning agricultural enterprises
- Now in it's 14th year
- 300+ investments made, over \$13 million invested
- Joint venture of Farm Credit East, CoBank, and Yankee Farm Credit



Many
Options are
Available



The Farm Credit System
(Farm Credit East)



Farm Service Agency



Seller



Commercial Banks

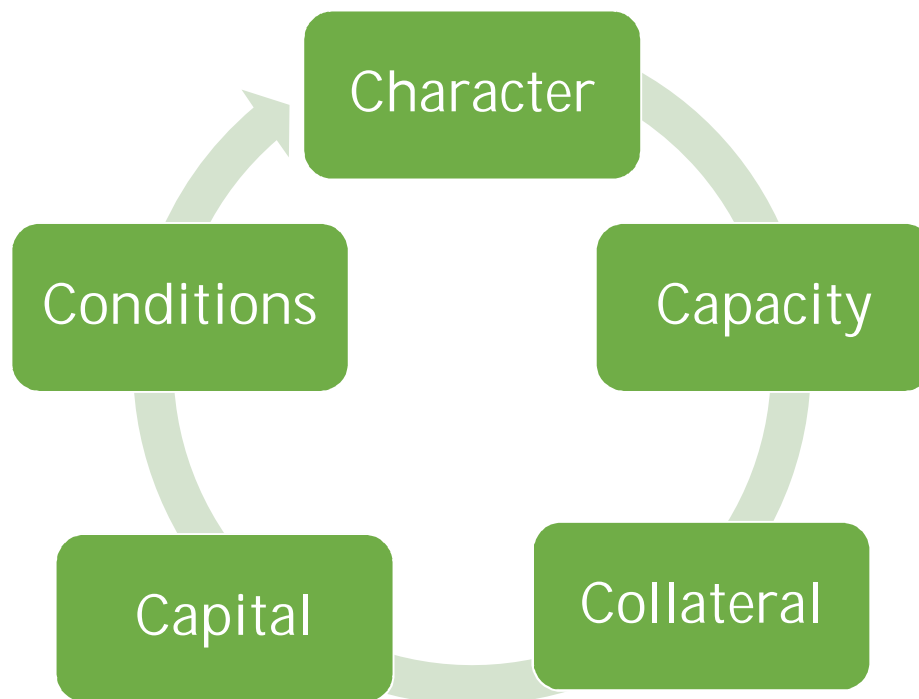


Angel Investor or Non-Profit



Community Development Corporations /
Economic Development Agencies

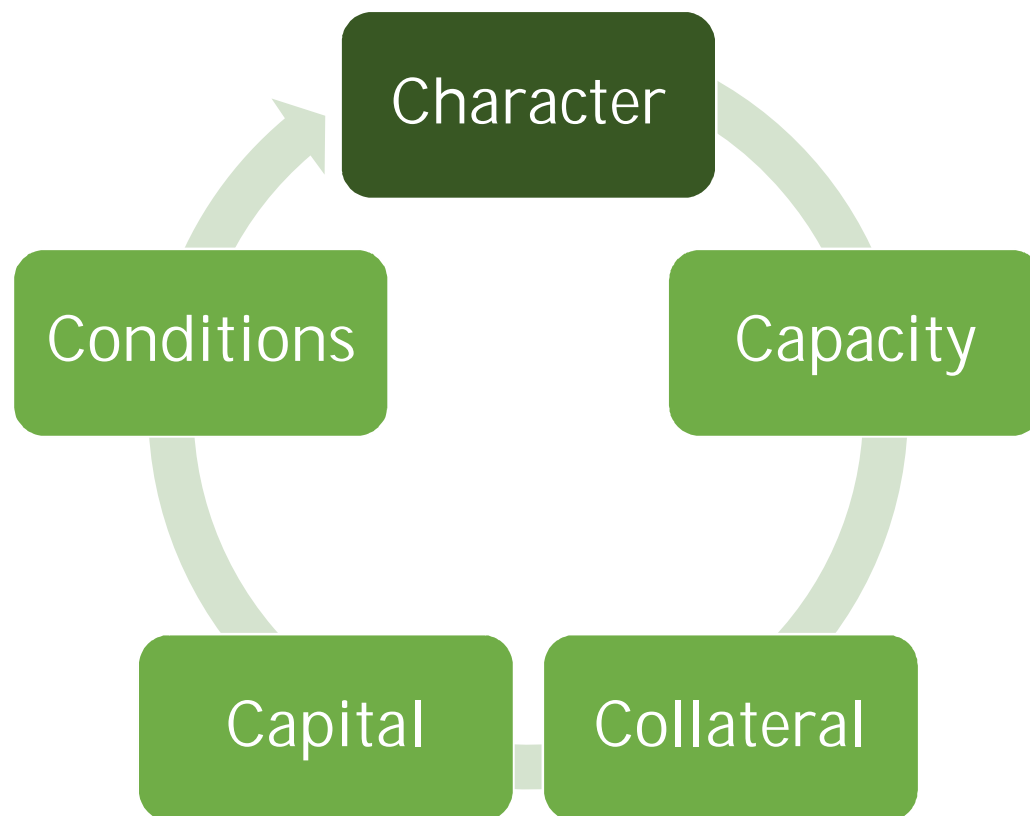
What a Farm Lender Looks For: The 5 "C's" of Credit



Character

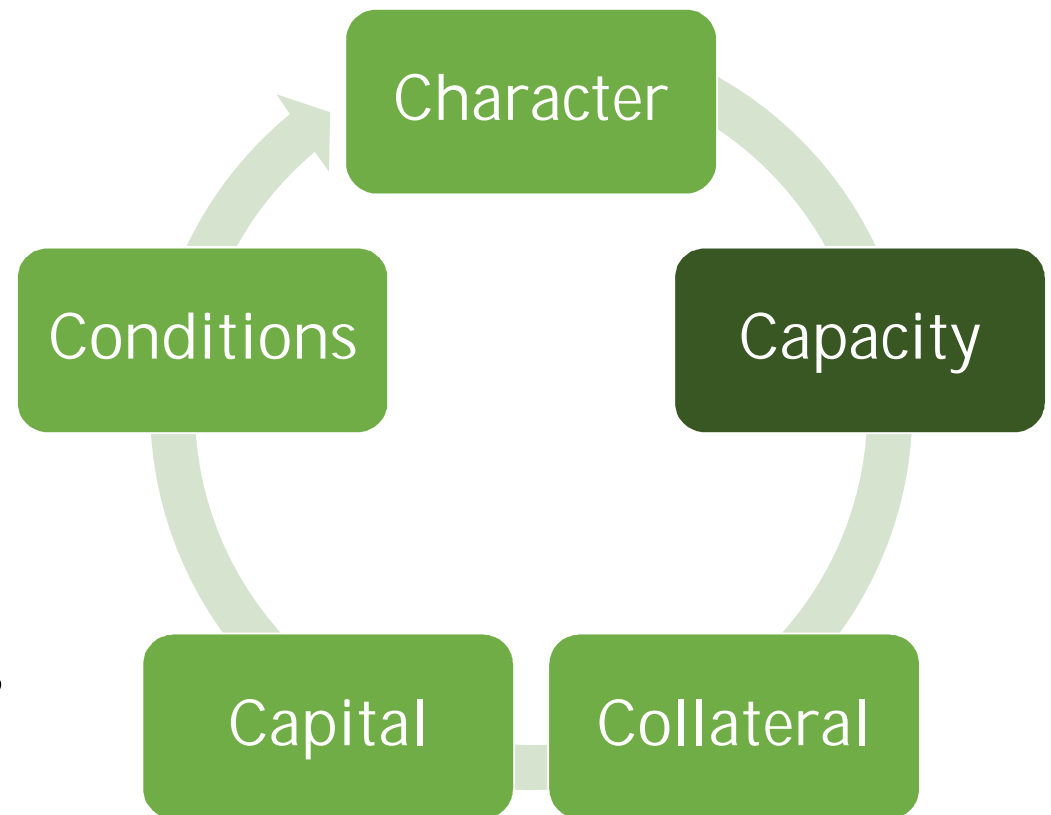
Credit Score (should be 700+)

- Demonstrates performance on past loans
- Indicates existing debt
- Know what is on your report
- Share and explain any problems that exist.
- AnnualCreditReport.com
- CreditKarma.com



Capacity to Repay

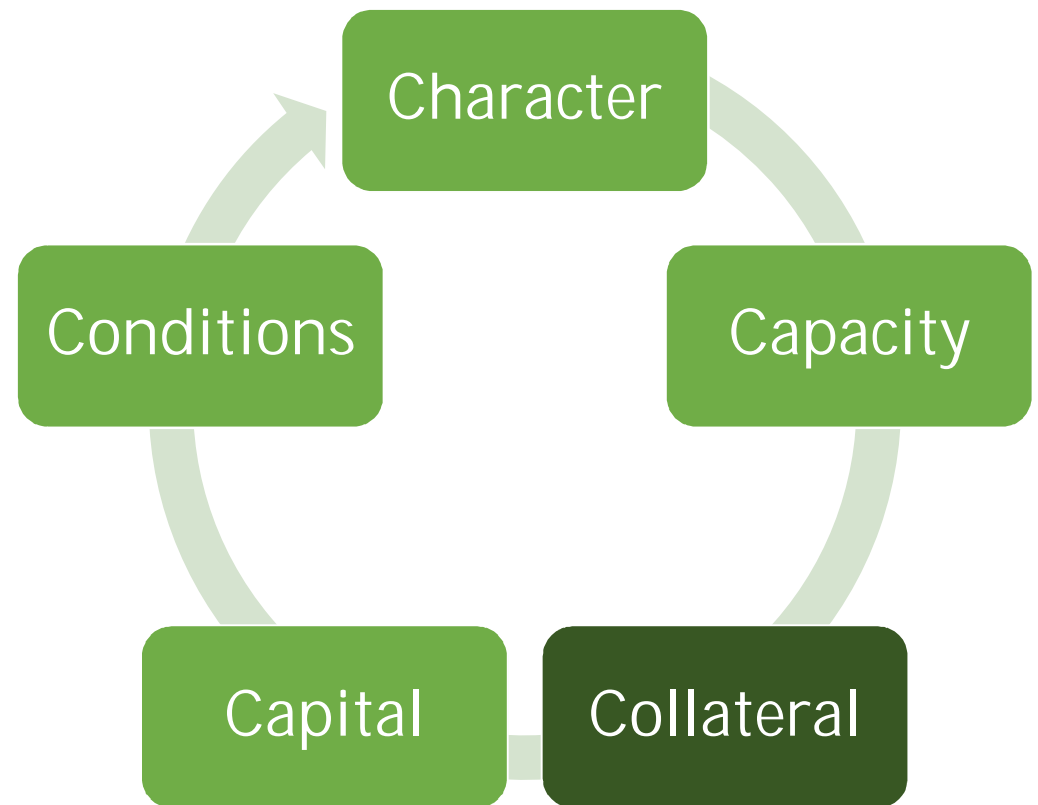
- How will you repay the loan?
- What are your earnings today?
- What will they be after the investment?
- History is important:
 - Income statements
 - Cash flow statements
 - Tax returns
- Projections & Budgets
- What if things don't go as planned?
- Off-farm income may be important



Collateral

The Lender's Fall Back Position

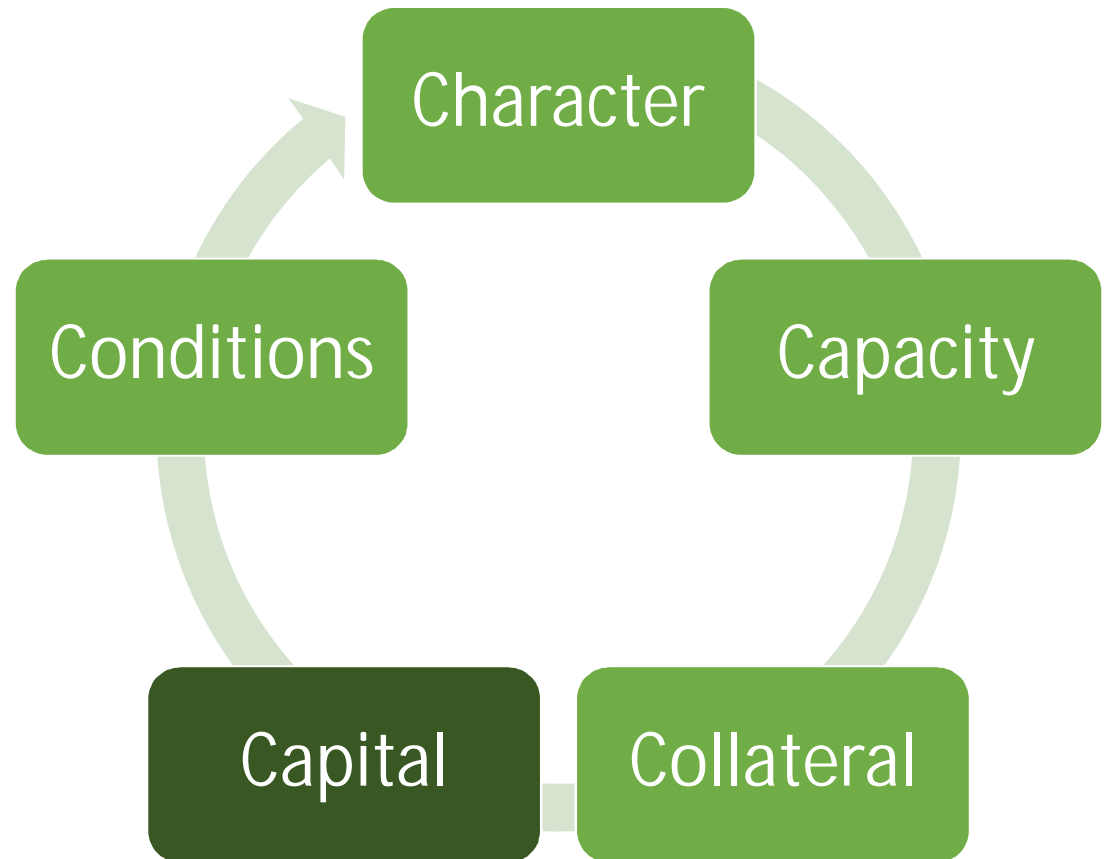
- Real estate is best
 - Livestock
 - Machinery/Equipment
 - Inventory
- What is it really worth?
 - Fair market value (FMV)
 - Net recovery value (NRV)
 - What will it get at auction?



Capital

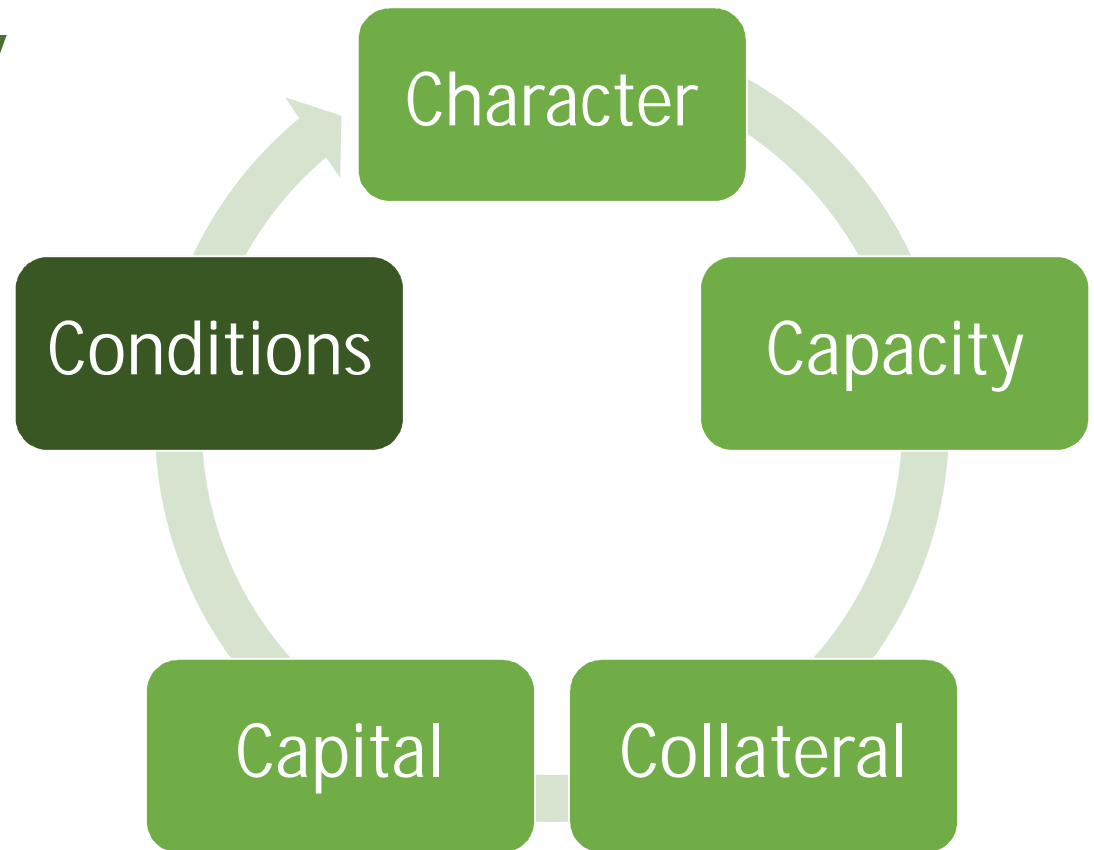
Do you have skin in the game?

- Net Worth
 - Debt-to-Asset Ratio
- How much do you own net of debt?
- Market value vs. Book value
- Balance Sheet



Conditions – “The Deal”

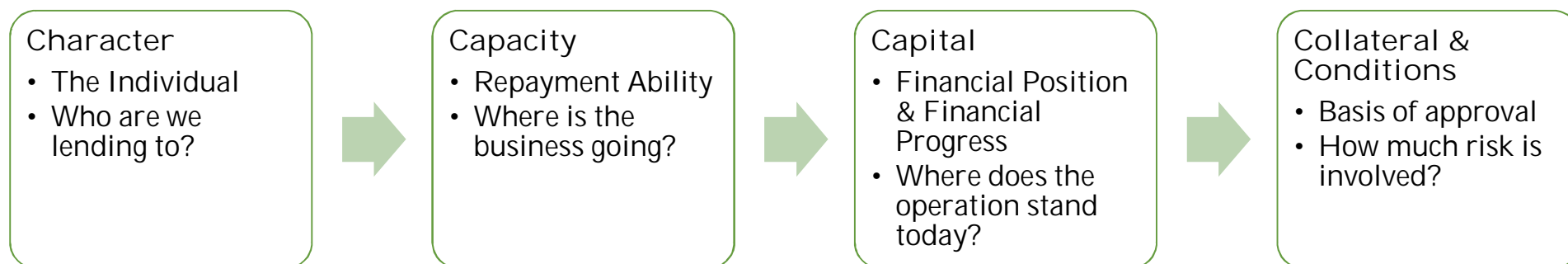
- Terms of the loan:
 - Real Estate 10-30 years
 - Machinery/Equipment 3-7 years
 - Livestock 1-3 years
 - Inventory – less than 1 year
- Loan term should be shorter than the life of the asset financed



How do lenders arrive at a decision?

Multiple considerations

Different lenders weigh criteria differently



"1 more year of payments and she's all mine!"



Don't finance beyond the useful life of an asset.

Don't Borrow Your Last Dollar



Cost overruns happen – don't get caught!

Capitalizing Operational Losses



What will change so you won't do it again next year?

Lack of Commitment



When the “going gets tough” the tough stick it out!

Lender “turn-offs”

- Poor records
- High existing debt
- Low credit scores
- Relying too much on collateral
 - not enough earnings
- Low personal investment
- Unrealistic expectations
- No “plan-B”, i.e. What if?...
 - Prices fall
 - The weather doesn’t cooperate
 - A buyer goes away
- “Build it and they will come” business plans
- Lack of cooperation & commitment when times get tough

We’re in it for keeps - you need to be too!

Thank you!



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