



Financial Fitness for Farmers Part 1

Balance Sheets

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Today's Presenter



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What is a Balance Sheet?



Joel Salatin



Balance Sheet Defined

- Summarizes the financial condition of your farm at one point in time.

It is a **SNAPSHOT**.





What does a Balance Sheet do?

- It estimates your NET WORTH
 - Most transactions affect your balance sheet
 - Therefore, it can change daily



What is the purpose of a Balance Sheet?

- It calculates the value of everything you **OWN** as well as everything you **OWE**.
- The difference between the two is your **net worth** (also called **owner equity**).
- $\text{Owner Equity} = \text{Assets} - \text{Liabilities}$



Definitions

- **Asset** – anything of value that you **own**.
- **Liability** – a debt or other financial obligation **owed** to someone else.
- **Owner Equity/Net worth** – total liabilities minus total assets.



Balance Sheet defined

- “Balance” idea:

$$\text{Owner Equity} = \text{Assets} - \text{Liabilities}$$





Balance Sheet example

- Let's say the only asset you have is a tractor. It is worth \$5,000. You paid \$1,000 down on it TODAY.
- What is your net worth?





Balance Sheet Format

Assets

A tractor worth \$5,000



Liabilities

\$4,000 owing on tractor

Owner's equity

$$\begin{aligned} \$5,000 - \$4,000 \\ = \$1,000 \end{aligned}$$

Assets – Liabilities = Owner's Equity (Net Worth)



Balance Sheet Format

Assets

A tractor worth \$5,000

\$5,000

Liabilities

\$4,000 owing

Owner's equity

\$1,000

\$5,000

It balances because liabilities
PLUS owner's equity = assets



Definitions: Assets

- An asset is anything of value that is owned
 - It can be sold to generate cash
 - It is typically used to produce other goods
 - Land
 - Livestock





Definitions: Current Assets

- Goods that have already been produced and can easily be sold
 - Hay
 - Produce
 - Livestock (not breeding stock)



Definitions: Noncurrent Assets

- More difficult to sell quickly and easily at their full market value—they are NOT liquid.
 - Machinery and equipment
 - Breeding livestock
 - Buildings
 - Land



Definitions: Liabilities

- An obligation or debt owed to someone else.
- An outsider's claim against one or more assets of the business, like accrued taxes.

IOU \$\$\$



Definitions: Current Liabilities

- Financial obligations that will become due and payable within 1 year:
 - Accounts payable
 - Loan payments due this year



Definitions: Noncurrent Liabilities

- Obligations that don't have to be paid in full within the next year.
 - The remaining balance on long-term debt.



Definitions: Owner Equity

- The amount of money left for the owner if the assets were sold and all liabilities paid.
- Also called **Net Worth**.
- The owner's current investment in the business.
- **Owner Equity = Total Assets - Total Liabilities**



What would change your owner equity?

- If the value of an asset changed
- If something is added or withdrawn from the business
 - Cash withdrawal
 - You receive an inheritance



What would **NOT** change your owner equity?

- Paying a debt
 - You are withdrawing funds from an asset (bank account)
 - You are reducing a liability
 - The asset goes down by the same amount as the liability
 - No change in owner equity!



Balance Sheet Analysis

- Compares your business to similar businesses
- Allows you to see how your business is doing over time
- Lenders use these to make lending decisions and monitor your financial progress



Balance Sheet Analysis: Debt to Asset Ratio

- $(\text{Total Debt}) / (\text{Total Assets})$
- Tractor example:
- $\$4,000 / \$5,000$
- .80





Balance Sheet Analysis: Debt to Asset Ratio

- Ideally your liabilities make up no more than half of the total value of your assets
 - Debt:Asset ratio ≤ 0.50
- A high debt:asset ratio makes you a riskier client for a bank lender



Balance Sheet Analysis: Equity to Asset Ratio

- $(\text{Total Equity}) / (\text{Total Assets})$
- Tractor example:
- $\$1,000 / \$5,000$
- .20





Balance Sheet Analysis: Equity to Asset Ratio

- Ideally your equity makes up more than half of the total value of your assets
 - **Equity:Asset ratio ≥ 0.50**
- A high Equity:Asset ratio makes you a less risky client for a bank lender



Solvency versus liquidity

- The previous two ratios are measures of solvency
- They examine the proportions of debt to assets and equity to assets



Liquidity measures

- Measures your ability to meet cash flow needs
- Current ratio: $(\text{current assets}) / (\text{current liabilities})$
- Working capital:
 $\text{current assets} - \text{current liabilities}$



Liquidity measures: Current ratio

- $(\text{current assets}) / (\text{current liabilities})$
- Ideally greater than one
- Since it's a relative measure, it is the same for both large and small businesses



Liquidity measures: Working capital

- Current assets - Current liabilities
- You need a comfortable margin in order to insure that you can meet your debts as they come due
- Appropriate amounts dependent on size
 - Large farms need more working capital



Summary

- A balance sheet measures the financial position of a business at a single point in time
- Ratios of debt:equity and assets:equity compare your firm to others, regardless of size



Exercise:

Balance Sheet for a sheep farm

Balance Sheet: Kate's Rambouillet Sheep Farm					
			Year		
Assets			1/1/2019	1/1/2020	
<i>Current Assets</i>					
		Cash & checking	\$2,200	\$1,200	
		Prepaid feed & supplies	\$750	\$1,950	
		Accounts receivable	\$200	\$0	
		Crops			
		Handspinning fleece	\$480	\$1,280	
		Fat lambs	\$800	\$1,800	
<i>Total Current Assets</i>			<i>\$4,430</i>	<i>\$6,230</i>	



Year-to-year changes

	<i>Intermediate Assets</i>				
	Breeding livestock	\$6,500		\$6,320	
	Trained working dog	\$1,000		\$800	
	Machinery	\$4,500		\$4,200	
	Titled vehicles	\$8,500		\$7,900	
	<i>Total Intermediate Assets</i>	<i>\$20,500</i>		<i>\$19,220</i>	



Year-to-year changes

	<i>Long Term Assets</i>				
	Land		\$125,000	\$125,000	
	Barn, fences		\$25,000	\$23,750	
	<i>Total Long Term Assets</i>		<i>\$150,000</i>	<i>\$148,750</i>	
	<i>Total Farm Assets</i>		\$174,930	\$174,200	
	<i>Personal Assets</i>		\$35,000	\$35,000	



		Year	
Assets		1/1/2019	1/1/2020
<i>Current Assets</i>			
	Cash & checking	\$2,200	\$1,200
	Prepaid feed & supplies	\$750	\$1,950
	Accounts receivable	\$200	\$0
<i>Crops</i>			
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<i>Total Intermediate Assets</i>		<i>\$20,500</i>	<i>\$19,220</i>
<i>Long Term Assets</i>			
	Land	\$125,000	\$125,000
	Barn, fences	\$25,000	\$23,750
<i>Total Long Term Assets</i>		<i>\$150,000</i>	<i>\$148,750</i>
<i>Total Farm Assets</i>		<i>\$174,930</i>	<i>\$174,200</i>
<i>Personal Assets</i>		<i>\$35,000</i>	<i>\$35,000</i>
Total Assets		\$209,930	\$209,200

**Asset
changes,
2019 to
2020**



Year-to-year changes, liabilities

Liabilities				
	<i>Current Liabilities</i>			
		Accrued interest		
		Machinery	\$306	\$306
		Mortgage	\$3,500	\$3,250
	<i>Total Current Liabilities</i>		<i>\$3,806</i>	<i>\$3,556</i>
	<i>Intermediate Liabilities</i>			
		Machinery	\$4,875	\$3,625
	<i>Total Intermediate Liabilities</i>		<i>\$4,875</i>	<i>\$3,625</i>



Year-to-year changes, liabilities

	<i>Long Term Liabilities</i>			
		Mortgage	\$70,000	\$65,000
	<i>Total Long Term Liabilities</i>		<i>\$70,000</i>	<i>\$65,000</i>
	<i>Total Farm Liabilities</i>		\$78,681	\$72,181
	<i>Total Personal Liabilities</i>		\$5,800	\$4,800
	Total Liabilities		\$84,481	\$76,981



Impacts of 2019-2020 changes

Net Worth		\$125,449.00	\$132,219.00	
Net Worth Change				\$6,770
Total Liabilities + Net Worth		\$209,930.00	\$209,200.00	
Total Debt to Asset Ratio		40%	37%	

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■ You Provide:

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 - Income Statement
 - All past year's expenditures & incomes
- Time & place most convenient to you

■ In Return:

- Whole Farm Financial Analysis
- Free trial of FINPACK with training
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