

Benchmarking – What Can We Learn from Others?

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Ever wonder why or how the neighbor down the road seems to keep growing their farm business year over year? Why is it that your cost of production is higher than what you hear or see as an average for your area? Are your financial records organized, summarized and analyzed in a way that allows making comparisons of your ag business financial data to those that have similar size farms and enterprises?

While we aren't able to know financial details about any one individual farm or ranch (other than our own), we can utilize information from a peer group of similar operations to help us improve our own operation. Organizing our farm and ranch production and financial data and then utilizing this information to look back historically and to benchmark with others, provides a way to measure our operation's financial health. In turn, these measurements and comparisons can provide clues to assist in important management decisions.

Compiling data and financial records for your farm or ranch as a whole (or by enterprise) represents an important piece of information when making management decisions. Comparing your information to other similar size farms and ranches is called benchmarking. Recording actual costs at the end of the production cycle alongside expected cost projections in enterprise budgets can be useful in establishing subsequent budgets and useful in benchmarking by enterprise. While organizing financial information on a whole farm basis and/or by enterprise is valuable for decision making within the production year, another valuable source comes from looking at trends over time.

One explanation of benchmarking is that it is a form of "learning from others." There are standards of benchmarking that help align key financial results so "apples to apples" comparisons can be made from one set of data to the next. An organization such as Nebraska Farm Business, Inc. (NFBI, nfbi.net) utilizes benchmarking standards and dedicates resources to assisting their clients with annual farm financial records and enterprise analysis. NFBI services are fee-based. They publish annual reports, including summaries of aggregate data on whole farm profitability, enterprise information and financial figures with averages of all farms, top- and low-third profitable farms, plus many additional reports such as comparisons by size of gross cash farm income, operator age, debt to asset ratio, total crop acres and comparison trends. In addition, NFBI provides their aggregate data to a national benchmarking database called FINBIN, which can be accessed at: finbin.umn.edu

Whole Farm Financial Benchmarking, an Example

For 2020, FINBIN (finbin.umn.edu) provided financial information on over 3,000 farms from seven states, including Nebraska. FINBIN reports that for 2020, average net farm income for all farms in their database was \$107,422 which was up over \$39,000 from 2019. FINBIN reported the average farm net worth of farms from all states that reported increased by \$192,000 with the term debt coverage ratio at 2.73 : 1 in 2020. From the NFBI 2020 report, average Net Accrual Farm Income for its clients was

\$232,117 with a positive change in earned net worth of \$179,118 and an average debt to asset ratio of 30% for 2020. And there are many more financial factors that are published in FINBIN and NFBI.

So how can you use this information to make a difference for your operation? First off, your farm financial records and yearly summary should be prepared using a similar methodology with adjustments made on an accrual basis if you use cash accounting, as most farm businesses do. After summarizing your information, farm financial standard measures can be calculated. Those standards fall into the following five categories as reported by NFBI with various ratios and guidelines included for each category:

- 1) Liquidity measures (ability to meet financial obligations as they are due)
- 2) Solvency (capacity to pay all business debts if the business was sold now)
- 3) Profitability (difference between the value of farm products produced and the cost to raise the products)
- 4) Efficiency (effective use of business assets to generate income)
- 5) Repayment capacity (ability to repay term debts on time)

Understanding how your operation might differ from the average or low- or high-third profitable farms that are included in benchmarking reports may be helpful. While there are many questions and answers to seek using benchmarking, you should start with a relatively short list of information that you'd like to know from benchmarking. Sample questions while considering the whole farm picture might include:

- How does your gross farm income stack up against total operating expenses?
- Is your farm on a smaller scale? If so, what difference does that make?
- Does your farm business carry more debt, and how does the debt load measure up with total assets in the operation or the business equity?
- How efficiently do your capital assets help produce income compared to other farm businesses?

If we can address these questions and others through benchmarking, we might see areas where financial improvements can be made.

Benchmarking Enterprises

Enterprise benchmarking for many represents a good way to start. Reviewing yield data and then going deeper to understand differences in enterprise profit margins might provide clues to changes that might be made with the goal of making improvements that add profitability to our bottom-line. Examples of common questions that might be asked as benchmarking is done on an enterprise basis are:

- How do my actual crop yields compare? Or is my weaning rate in my cow herd on par with others?
- Are other farms in the benchmark group marketing their crops or livestock for a higher price? If so, can we start to understand their method(s) in doing so?
- Are there certain material input costs that show a much lower cost figure than what your enterprises show? What is their chemical and fertilizer costs per acre versus yours for the same crop?
- In the case of livestock, are their production and sales figures are higher, yet their vet expense is higher? If so, why might that be?
- Are your costs per unit of production trending the right way in your favor, when compared to similar operations with similar enterprises?

To benefit the most from financial benchmarking, your business records and data must be organized so you can study your business information, set up trend data comparisons over several years and make benchmark measurements from peer group data. Utilizing the financial analysis services of an

organization like the NFBI and joining as a member is an excellent way of utilizing benchmarking in Nebraska. Just as we personally want to watch our health, our business health is important to track. Benchmarking provides additional information to guide us in making decisions to sustain or grow a healthy operation.

Sources:

FINBIN Whole Farm Summary Report, <https://finbin.umn.edu/CommonOpts/PickStates>

2020 Whole State Average Farm Financial Data, Nebraska Farm Business, Inc., nfb.net

Barrett, Tina, Good Farmer to Great Manager, Understanding Good Records, 2019, Nebraska Farm Business, Inc.

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