Financial Health Check

Jessica Groskopf, Extension Educator
308-632-1247 jgroskopf2@unl.edu
Balance Sheet

• A snapshot of your business’s financial position at a point in time.

• Listing of everything your business owns and owes.

• Required when applying for a loan.
• Helps guide decision making.
Balance Sheet
Prepare your balance sheet at the same time every year.
Balance Sheet
Everything the business owns.
Keep your business & personal separate.
**Assets**

- Cash
- Checking Accounts
- Prepaid expenses & supplies on hand
- Investment in growing crops
- Accounts receivable
- Hedging accounts
- Crops “in bin” and market livestock
- Breeding livestock
- Machinery
- Titled vehicles
- Land
- Buildings/Improvements
Assets: cost vs. market

• Put a value on it...
  • Cost value
  • Market value
Assets: cost vs. market

- **Cost value** - purchase price less *economic* depreciation

- Depreciation – “wear and tear” overtime that depletes the value of an asset: machinery, vehicles, buildings, breeding livestock.

- Depreciation reported on the balance sheet is sometimes called “Book depreciation”
  - Maybe different than depreciation reported on taxes – may be “accelerated” to reduce income tax liability (Section 179).

**Straight-line depreciation** = \( \frac{Purchase\ Price - Salvage\ Value}{Asset\ Life} \)

\[
\frac{$75,000 - $15,000}{10} = 6,000/\text{per year}
\]
Put a value on it…

- Cost value – purchase price less *economic* depreciation

- Market value – what a willing buyer would pay for the asset
Assets: cost vs. market

• Put a value on it...
  • Cost value – purchase price less *economic* depreciation

• Market value – what a willing buyer would pay for the asset

<table>
<thead>
<tr>
<th>Land (Schd M)</th>
<th>Acres</th>
<th>Cost Value</th>
<th>Market Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Farm 1</td>
<td>235</td>
<td>152,750</td>
<td>293,750</td>
</tr>
<tr>
<td>Farm 2</td>
<td>160</td>
<td>32,000</td>
<td>224,000</td>
</tr>
</tbody>
</table>
Balance Sheet
Take care when valuing assets. Make notes when you adjust values.
Everything the business owes.

<table>
<thead>
<tr>
<th>Assets</th>
<th>Liabilities</th>
</tr>
</thead>
<tbody>
<tr>
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<tr>
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</tr>
</tbody>
</table>
Liabilities

- Accrued interest
- Accounts Payable
- Operating loans/lines of credit
- Credit cards
- Machinery Loans
- Land Loans
<table>
<thead>
<tr>
<th>Assets</th>
<th>Liabilities</th>
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</thead>
<tbody>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Organize

• Current (< 1 year)
• Intermediate (1-10 years)
• Long-term (>10 years)

... and subtotal
Organize

• Current (< 1 year)
• Intermediate (1-10 years)
• Long-term (>10 years)

... and total
Assets

Current
- Cash
- Checking Accounts
- Prepaid expenses & supplies on hand
- Investment in growing crops
- Accounts receivable
- Hedging accounts
- Crops “in bin” and market livestock

Intermediate
- Breeding livestock
- Machinery
- Titled vehicles

Long-term
- Land
- Buildings/Improvements
Liabilities

Current
• Accrued interest
• Accounts Payable
• Operating loans/lines of credit
• Credit cards
• Current portions of intermediate and long-term loans

Intermediate
• Machinery Loans

Long-term
• Land Loans
Net Worth

The difference between, assets and liabilities.

\[ \text{Total Assets} - \text{Total Liabilities} \]

“Owner’s equity” in the business. Value of what the owner’s have in the company.
Farm Financial Standards Council - provides standard financial guidelines for farms/ranches

- Allow for comparison across businesses
- Monitor financial health
- Measure financial performance

Currently 21 measures
Ratios...

• **Liquidity Measure** – is the ability of a business to meet financial obligations as they come due.
  - Working capital
  - Current ratio

• **Solvency Measure** – the ability of a business to pay all of its debts if it were sold tomorrow.
  - Debt to asset ratio

• **Profitability** – the difference between the value of goods produced and the cost of their production.
Ratios...

• Working Capital
• Current Ratio
• Total Debt to Asset
Working Capital

Liquidity Measure – ability to meet short-term obligations, expressed in $.

Current Assets – Current Liabilities

Can the business cash flow in the near term?

\[
\text{Assets} = \text{Liabilities} + \text{Net Worth}
\]
Current Ratio

Liquidity Measure – ability to meet short-term obligations, expressed as a %.

\[
\frac{\text{Current Assets}}{\text{Current Liabilities}}
\]

“You/I have $X.XX assets to cover each $1.00 of liabilities” (the bigger the better).

<1.1  1.1 -1.7  >1.7
Debt/Asset Ratio

Solvency Measure – the ability of a business to pay off all of its debts.

\[
\frac{\text{Total Liabilities}}{\text{Total Assets}}
\]

How much of the business the bank owns (smaller the better).

<table>
<thead>
<tr>
<th>&gt;60%</th>
<th>20-60%</th>
<th>&lt;20%</th>
</tr>
</thead>
</table>

Balance Sheet

<table>
<thead>
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<tbody>
<tr>
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<td>Intermediate</td>
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</tr>
<tr>
<td>Long-term</td>
<td></td>
</tr>
</tbody>
</table>

\[\text{Assets} = \text{Liabilities} + \text{Net Worth}\]
### An Example

<table>
<thead>
<tr>
<th>Assets</th>
<th>Liabilities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Assets = $100,000</td>
<td>Current Liabilities = $90,000</td>
</tr>
<tr>
<td>Intermediate Assets = $900,000</td>
<td>Intermediate Liabilities = $410,000</td>
</tr>
<tr>
<td>Long Term Assets = $4,000,000</td>
<td>Long Term Liabilities = $2,000,000</td>
</tr>
<tr>
<td>Total Assets = $5,000,000</td>
<td>Total Liabilities + Net Worth = $5,000,000</td>
</tr>
</tbody>
</table>

**Working Capital**: $10,000

**Current Ratio**: 1.1, 1.4, 1.7

**Debt to Asset**: 40%, 50%, 60%
What should I do with $10,000?

1. Put in current assets
2. Pay-off current liabilities
3. Put in intermediate assets
## Financial Statements

<table>
<thead>
<tr>
<th>Assets</th>
<th>Liabilities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Assets = $110,000</td>
<td>Current Liabilities = $90,000</td>
</tr>
<tr>
<td>Intermediate Assets = $900,000</td>
<td>Intermediate Liabilities = $410,000</td>
</tr>
<tr>
<td>Long Term Assets = $4,000,000</td>
<td>Long Term Liabilities = $2,000,000</td>
</tr>
<tr>
<td>Total Assets = $5,010,000</td>
<td>Total Liabilities = $2,500,000</td>
</tr>
<tr>
<td>Total Liabilities + Net Worth = $5,010,000</td>
<td>Net Worth = $2,510,000</td>
</tr>
</tbody>
</table>

## Ratios

- **Current Ratio**
  - 1.1
  - 1.4
  - 1.7

- **Debt to Asset**
  - 40%
  - 49.9%
  - 60%

- **Working Capital**
  - $20,000
Payoff $10,000 in current liabilities

<table>
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<tbody>
<tr>
<td>Current Assets = $100,000</td>
<td>Current Liabilities = $80,000</td>
</tr>
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<td>Intermediate Liabilities = $410,000</td>
</tr>
<tr>
<td>Long Term Assets = $4,000,000</td>
<td>Long Term Liabilities = $2,000,000</td>
</tr>
<tr>
<td>Total Assets = $5,000,000</td>
<td>Total Liabilities = $2,490,000</td>
</tr>
</tbody>
</table>

Total Liabilities + Net Worth = $5,000,000

Working Capital = $20,000

Current Ratio: 1.1, 1.25, 1.4, 1.7

Debt to Asset: 40%, 49.8%, 60%
Put $10,000 in intermediate assets

<table>
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<tbody>
<tr>
<td><strong>Current Assets</strong></td>
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</tr>
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<td><strong>Total Assets</strong></td>
<td><strong>Total Liabilities + Net Worth</strong></td>
</tr>
<tr>
<td>$5,010,000</td>
<td>$5,010,000</td>
</tr>
</tbody>
</table>

- **Working Capital**: $10,000
- **Current Ratio**: 1.1
- **Debt to Asset**: 49.9%

Net Worth: $2,510,000
## Summary

<table>
<thead>
<tr>
<th>Action</th>
<th>Working Capital</th>
<th>Current Ratio</th>
<th>Debt to Asset</th>
</tr>
</thead>
<tbody>
<tr>
<td>START</td>
<td>$10,000</td>
<td>1.1</td>
<td>50%</td>
</tr>
<tr>
<td>Add $10,000 to current assets</td>
<td>$20,000</td>
<td>1.22</td>
<td>50%</td>
</tr>
<tr>
<td>Pay off $10,000 in current debt</td>
<td>$20,000</td>
<td>1.25</td>
<td>50%</td>
</tr>
<tr>
<td>Buy a $10,000 in intermediate assets</td>
<td>$10,000</td>
<td>1.1</td>
<td>50%</td>
</tr>
</tbody>
</table>
Improving your balance sheet..

Assets

Liabilities
Improving your balance sheet..

- Sell assets for more than they are valued for on the balance sheet
- Pay off debt
- Refinance
  - Reduce interest expense, or extend length of the loan
- Delay capital purchases
- Reduce personal withdrawals
- Sell off unprofitable or unnecessary assets – use assets more efficiently (custom farming)
https://mosesorganic.org/fearless-farm-finances/