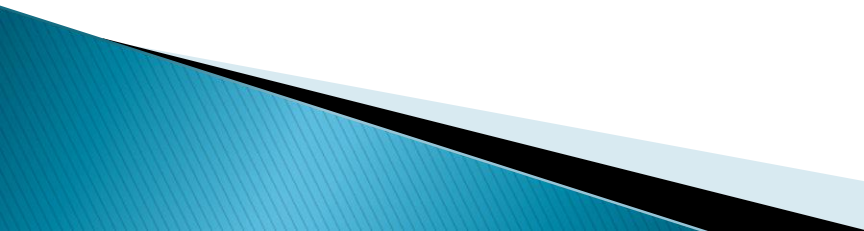


# Farm Business Financial Management

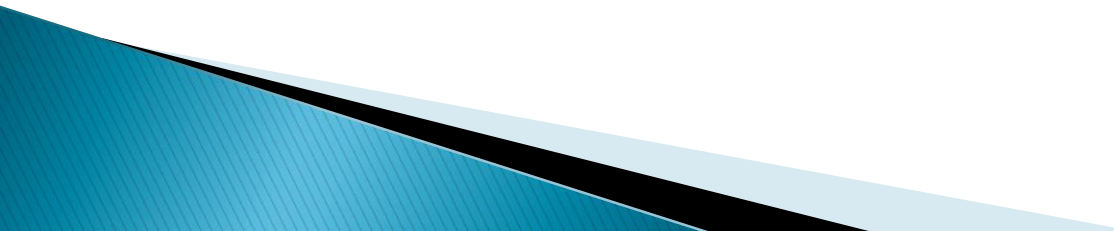
FINANCIAL PLANNING



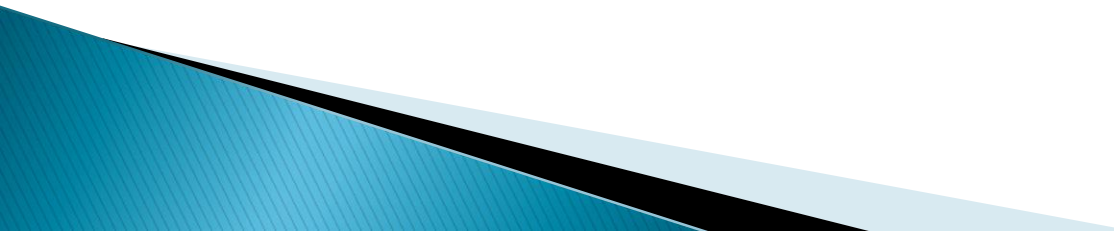
# KEY POINTS

- ▶ Appreciate the importance of financial management in a farming business
  - ▶ Understand and appreciate the essence of enterprise budgeting
  - ▶ Prepare a simple enterprise budget
  - ▶ Understand the purpose of break even analysis
  - ▶ Calculate the breakeven price and yield
  - ▶ Prepare a basic cash flow budget
- 

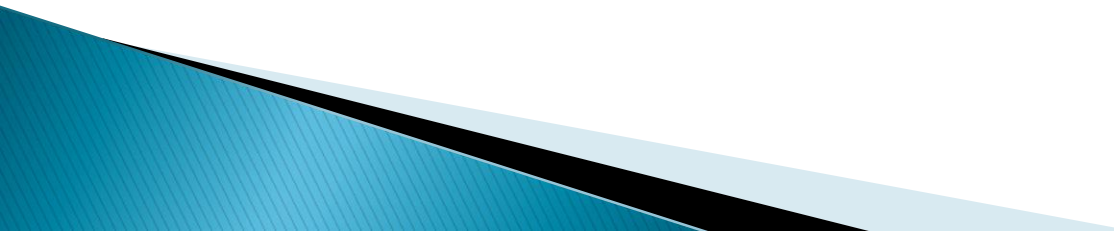
# What is farming business financial management?

- ▶ means using limited financial resources in a way that maximizes your return or profit.
  - ▶ It involves *planning, organising, directing* and *controlling* the financial activities such as sourcing and utilisation of funds for business to ensure:
    1. Adequate supply of funds for the business
    2. Optimum use of funds
    3. Proper investment of the funds
- 

# Key functions of Farm financial management include :

- ▶ Estimation of capital requirements basing on anticipated costs and possible returns
  - ▶ Making a decision on sources of funds (loans and equity)
  - ▶ Investment of funds (decisions on the best rewarding enterprises)
  - ▶ Utilisation of the farming business profits
  - ▶ Building stocks over time
  - ▶ Management of finances (wages overheads, purchases, loan repayments )etc.
  - ▶ Cash flow projections
  - ▶ Control of funds
- 

# Financial management tools every farmer should USE:

- ▶ Enterprise Gross Margin budget
  - ▶ Whole farm budget
  - ▶ Partial budget
  - ▶ Break even analysis
  - ▶ Cash flow budget
  - ▶ Sensitivity analysis
- 

# Budgeting

- ▶ ***NO FARM CAN OPERATE WITHOUT BUDGETS!***
- ▶ In making a decision among alternatives, the farmer usually looks at the future outcomes of the different possible choices to come up with a plan which will increase his / her profit.

# Budgets are used to:

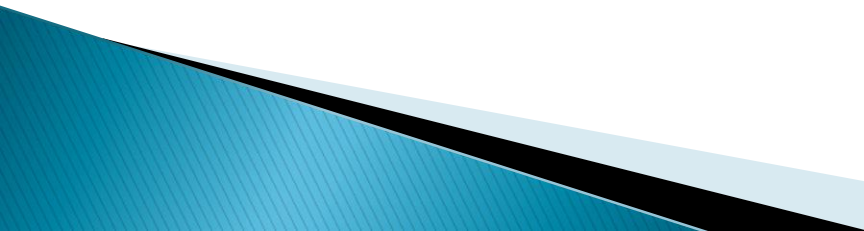
- ▶ Decide what, how and when to produce,
- ▶ Itemize the financial aspects of the farming business e.g. expected receipts (income) as well as expected costs and therefore determine profit
- ▶ List the inputs and production practices required by an enterprise
- ▶ Evaluate the performance of different farm enterprises
- ▶ Estimate benefits and costs for changes in production practices
- ▶ Provide the basis for a total farm plan
- ▶ Show the capacity of the farming business to carry the risk
- ▶ Support applications for credit (Show the ability of the business to pay the debt)
- ▶ Inform all interested parties of the costs incurred in producing an agricultural product
- ▶

# Enterprise Budget

Opening Stock (start of year)				Closing Stock (end of year)		
No	Value	Total	Class of stock	No	Value	Total
2	2,000	4,000	Bulls	2	2,000	4,000
20	400	8,000	Breeding Cows	25	400	10,000
5	300	1,500	Bulled heifers	7	300	2,100
15	200	3,000	Heifers 1-2 years	15	200	3,000
8	300	2,400	Steers 2+	8	300	2,400
8	200	1,600	Steers 1+	7	200	2,100
15	60	900	Calves	17	60	1,020
Birth 17 calves	-			Deaths 1 calf		
Purchases	-			Sales 8 Steers	350	2,800
Total (A)		21,400		(B)		27,420
Gross Income (A-B) Trading Profit		6,020				
		27,420	TOTAL			27,420



# Key terms used in Enterprise Gross Margin analysis

- ▶ ***Gross Income***
  - ▶ This is the total value of production from an enterprise
  - ▶ It includes sales, value of produce consumed at home, and value of retained produce.
  - ▶ ***Variable costs***
  - ▶ These are production costs that can be directly allocated to a particular enterprise in a production season and they change with the size and scale of production
  - ▶ Examples are stock feed costs, seed, fertilizers, labour, and agrochemicals
  - ▶ ***Gross Margin***
  - ▶ This is Gross Income less total variable costs
  - ▶ Is a measure of enterprise viability
- 

# Partial Budget

- ▶ Partial budget analysis is a marginal analysis that looks at changes that occur in costs and incomes because of marginal changes in a farm programme. It is used to calculate the expected change in profit for a proposed change in the farming business.

REDUCED COSTS (USD) Weeding labour = 600 Depreciation of hoes = 200	ADDITIONAL COSTS (USD) Depreciation of sprayer = 300 Purchase of chemical = 200 Protective clothing = 100
ADDITIONAL INCOME = Nil	REDUCED INCOME = Nil
TOTAL = USD 800	TOTAL = 600

# Break – even Analysis

- ▶ *breakeven analysis determines the level at which total revenue equals total cost.*
- ▶ A farmer may ask herself what optimum acreage say maize, she needs to produce viably ( **break – even area**)
- ▶ A farmer may also want to know the minimum price per kg that she should charge/ goat in order to cover production costs (**break – even price**)
- ▶ A farmer may also want to know the minimum yield/quantity she could expect per ha of luncene in order to cover the costs (break – even yield/quantity)

# Break – even production unit

- ▶ The minimum production unit (*area, herd size, batch size etc*) that a farmer should produce in order for him / her to cover all costs over and above variable costs at a given output price and yield.
- ▶ Break even area/herd size =  $\frac{\text{Total fixed costs}}{\text{gross margin}}$

# example

- ▶ A maize farmer has a gross margin per ha of USD300 and overheads of US\$ 6, 000. Given that the farmer is paying US\$ 4, 500 towards loan and interest per year, what is the number of hectares required to cover the costs per year.
- ▶ Gross margin per ha = 300
- ▶ Overheads = 6,000
- ▶ Loan payment = 4,500
- ▶ Total costs (over heads + loan repayment) = 10,500
- ▶ Break even number of ha =  
 $10,500/300$
- ▶ = 35
- ▶ Therefore, if the farmer produces on 35 hectares at the above costs and returns, he/she will just cover his/her variable costs, overhead costs and pay back the loan and interest.

# cash flow

- ▶ Cash flow budget is a forecast of the movement of money into (cash inflows) and out of (cash outflows) the farming business over a given period. A cash flow budget can be used to assess the timing, amount and predictability of future cash flows and it can be the basis for resource utilisation with time

END

