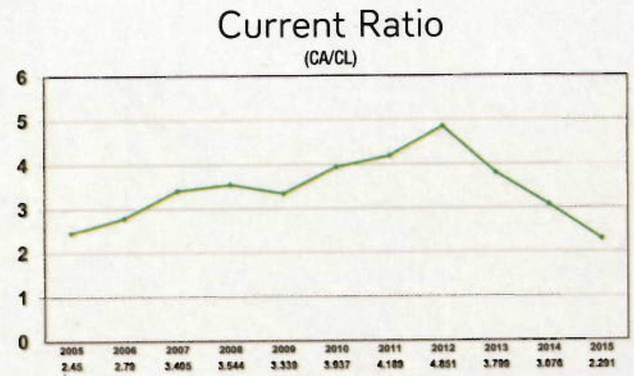
FINANCES

By Dan Looker

GOOD RECORDS BETTER FINANCIAL RECORDS WON'T CHANGE LOW PRICES, BUT THEY CAN HELP YOU KEEP LENDERS INFORMED.

Financial records can't work miracles. They won't raise low commodity prices. They can give you earlier warnings of potential problems, however, and a better chance of working them out with your lender, say experts in farm record keeping.

"We find that people who keep good records year in and year out are better financial managers because they're paying attention to those details," says Kent Vickre, state coordinator of the Iowa Farm Business Association (IFBA).



This ratio looks at the net payment obligation in the next 12 month from cash or assets quickly converted to cash.

Analysis: 2.0 Excellent. 1.5 Fair. 1.0 Weak

Current ratio, a measure of ability to pay debts, has weakened recently for IFBA members.

WHAT'S DRIVING KEY FINANCIAL RATIOS

We all know farm income is falling. For members of the IFBA, accrued net farm income is down from more than $300,000, on average, in 2012 to about $18,000 in 2015. That's driving three key financial ratios.

- **Current Ratio.** This measures your ability to pay debts. It divides cash and assets you can quickly sell by payments owed over the next 12 months. A ratio of 2 is considered excellent, 1.5 is fair, and 1 is weak. IFBA members still look good, with a 2.3 average ratio for 2015. It's far less than a ratio of almost 5 in 2012.
- **Debt-to-Asset Ratio.** This ratio of the portion of farm assets owed to creditors also looks good. Anything lower than 30% (.3) is rated excellent, 30% to 60% is fair, and above 60% is weak. In 2015, the ratio for IFBA members was still strong at .279. It's been trending higher since 2012, though.
- **Rate of Return on Equity.** This measure of net farm income (minus unpaid family labor) over farm net worth already raises a red flag. In 2015, it was .9 of 1% (anything below 2% is weak). In 2011, it was above 14%.

Vickre urges you to share such important measures with lenders. "Meet with your banker sooner rather than later to be abreast of the situation," he says. "We had some people who didn't get financed this year."

Forewarned lenders may have options such as lengthening terms of machinery loans and converting short-term notes to land mortgages. The American Bankers Association is urging farmers to discuss Farm Service Agency loan guarantees with lenders.

Improved record keeping doesn't have to be overly complicated.

"For management purposes, have a cash flow monthly budget," says Jeff Bushey, a CPA and managing partner with Nietzke & Faupel, PC in Pigeon, Michigan. You can do this on your own with good accounting software, says Bushey, a leader in the Farm Financial Standards Council.

Kent Vickre

Some lenders also want quarterly financial reports. In Bushey's region, that's not required for grain farmers with fewer than 10,000 acres.

Ultimately, the way you use records is key. Farmers are already cutting costs. IFBA records show the biggest costs are cash rent, machinery, fertilizer, and direct inputs, says Vickre.

Another sometimes touchy cost is living expenses. Vickre doesn't like to tell farmers where to cut family living, "but it definitely is an expense that has to be considered," he says. "If you can account for every dollar that goes for family living, that really helps with a banker."

Jeff Bushey

That helps up to a point, cautions Mark Holkup, associate professor of farm management education at Bismarck State College in North Dakota. "It's really hard to get a banker's sympathy if your family living is twice the average."

If you're fortunate enough to have income you want to offset with machinery depreciation this year, Holkup says you should still normally pay taxes on adjusted gross income that equals family living expenses.

Mark Holkup

"It's always cheaper for cash flow to pay the taxes than it is to borrow money to defer taxes," he says.

Every cost should be viewed critically.

"You need to look at that $30,000 cement pad you're pouring and ask, 'Can I do it?'" he says. Look at what share it is of your net income – not gross revenue.

Having financial snapshots this year could prevent costly errors in judgement.

"For a lot of folks, 2016 is going to be a watershed year," Holkup says.

Photography: Provided by Kent Vickre, Jeff Bushey, Mark Holkup