



**Getting on Track:**  
*Better Management through  
Basic Financial Statements*

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Provide a welcoming to Session One and to the course.

The objectives of the course are:

- Describe the purpose and characteristics of a “cash flow statement”
- Describe the purpose and characteristics of a “balance sheet”
- Describe the purpose and characteristics of an “income statement”
- Describe the purpose and characteristics of a “statement of owner equity”
- Understand the challenges and benefits of the four financial statements
- Learn how to create financial statements for your own business

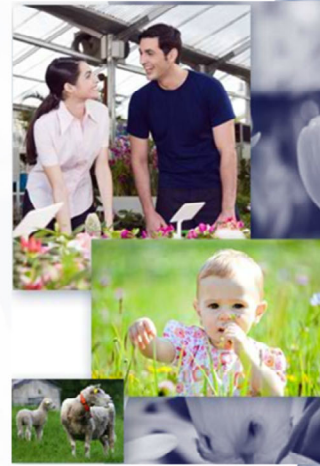
There will be five 45-minute to one-hour sessions. This section will last 60 minutes. In this session, we will discuss:

- Cash flow statements
- Cash inflows and outflows
- Personal and business cash inflows and cash outflows
- Estimating projected cash inflows
- Estimating projected cash outflows
- Calculating net cash flow
- Types of cash flow statements

## Meet Jack and Joanie

- **Current Situation:**

- Farm:
  - 10 acres
  - House, yard, garden, roads, and waste land
- Jobs:
  - Jack is a welder: \$50,000 per year
  - Joanie is an admin assistant: \$30,000 per year
- Family:
  - 18-month-old daughter
  - One more on the way
  - Can Joanie stay at home after the pregnancy?



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Jack and Joanie are a young couple in their late 20s living just down the road from her parents. They purchased a small property and trailer house from her aunt three years ago just after their wedding.

**Farm:** The property consists of ten acres of pastures and two acres used by the house, yard, garden, roads, and waste land. There is one small shed near the house in which they store their lawn mower and gardening tools. Another shed is located in the pasture.

**Jobs:** Jack works in the oil and gas fields as a welder earning \$50,000 per year. His monthly take home pay is \$3,200. Joanie currently works as an administrative assistant and earns about \$30,000 per year. Jack earns enough as a welder to cover ordinary family living expenses, but there is little money for extras. Joanie's income as an administrative assistant has allowed them to take a few trips, buy a fishing boat, and keep the house in good repair.

**Family:** Jack and Joanie have an 18-month-old daughter. Joanie is pregnant with their second child and would like to quit her job to be a stay-at-home mom. Jack supports her desire, but they both are worried about finances.

## Meet Jack and Joanie (cont.)

- **The Enterprise:**
  - The farm currently includes three ewes and a flower garden
  - They have given thought to either expanding their sheep flock or selling flowers as income if Joanie quits her job to stay at home with the children
- **Meet Dad:**
  - Joanie's dad is a loan officer and advises Jack and Joanie on managing their finances
- **Financial Statements:**
  - Cash flow statements
  - Balance sheets
  - Income statements
  - Statements of owner equity



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Jack's parents gave their granddaughter three ewes last Easter. Jack and Joanie would like to use them as a foundation for a small flock. The sheep could graze the pasture and help keep weeds under control. They could sell the wool and lambs that they produce. Joanie has a small garden to help feed the family. She also has several large flower beds located around the property from which she gives away many flowers. People say she has a “real knack” for raising a wide variety of unusual flowers. They have given thought to possibly expanding their sheep flock or selling flowers to allow Joanie to quit her job.

Joanie's dad is a loan officer. He has become a mentor to Jack and Joanie and provides them good advice about how to manage their money and make good financial decisions. Dad explains that Jack and Joanie can use some basic financial statements to help analyze the sheep and flower enterprises to determine if they generate enough income to allow Joanie to stay home. Financial statements are also useful to apply for a loan if necessary.

Additional teaching point: Enterprise refers to a set of activities that results in separate products produced by a farm/ranch. For example, on a ranch the hay enterprise can be separated from the cow/calf enterprise. On a farm, hay would be separated from beans. Hay would also be separated from beets and barley, even if they are grown in rotation with one another.

Let's follow Jack and Joanie as they learn about the four primary financial statements: cash flow statement, balance sheet, income statement, and statement of owner equity.

During these sessions, you will learn the purpose or use of each financial statement, the information contained in each, and instructions for how to build each document. You will also learn how financial statements can be used to make management decisions and measure financial performance. Let's begin today by learning about Cash Flow.

## Projected Cash Flow Statements

- **Definition:**

- Provides information on the business's ability to generate enough cash to meet financial obligations
- Helps to identify the sources of and uses for cash in the business
- Does NOT provide an estimate of the business profitability



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Jack and Joanie decide to explore the possibility of a flower business first. To start, Joanie's dad recommends that they create a projected cash flow statement to determine how much net cash inflow they can generate by selling flowers. But what is a cash flow statement?

A cash flow statement helps a business to plan for periods in which cash inflows exceed outflows, creating a cash surplus, and periods in which cash outflows exceed cash inflows, creating a cash deficit.

A cash flow statement does not provide an estimate of profit. Other financial statements are needed to calculate business profitability. Usually information in a cash flow statement is calculated by month, but it can be organized by another time period, such as quarterly or yearly, if desired.

Additional teaching note: Profitability, in the simplest definition, is revenue minus expenses.

Additional teaching moment: Print off and hand out the sample cash flow statement found on the CD and discuss with the class.

## How is a Cash Flow Statement Used?

<b>Business Managers</b>	Cash flow statements allow business managers to plan for times of cash surplus or when borrowed funds might be needed to cover cash deficits. They provide an early warning system for cash flow shortages.
<b>Borrowers</b>	Cash flow statements help a borrower determine the cash available for repaying debts.
<b>Lenders</b>	Cash flow statements help lenders analyze a proposed loan by showing the borrower's ability to generate sufficient cash to make payments without disrupting farm operations.



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Cash flow statements allow you to plan for when cash will be available or when borrowed funds might be needed. They provide an early warning system for cash flow shortages.

Cash flow statements help a borrower determine the cash available for repaying debts. Additionally, the information can be used to help explore alternative loan amounts, repayment lengths, and interest rates.

Cash flow statements help lenders analyze a proposed loan by showing the borrower's ability to generate sufficient cash to make payments without disrupting farm operations.

## How to Create a Cash Flow Statement

### Record cash inflow like the:

- Deposits in a check book
- Deposits on a bank statement
- Payments on a credit card statement

### Record cash outflows like the:

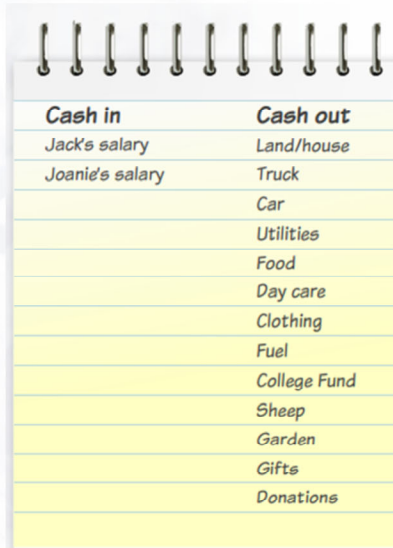
- Record of checks in a check book
- Withdrawals on a bank statement
- Charges on a credit card statement



You record cash inflows like a deposit is recorded in your checkbook or bank statement. Cash outflows are recorded like your record of checks, withdrawals on a bank statement, or charges on a credit card statement.

The level of detail can vary depending on the purpose of the statement but the format is always essentially the same.

## Step 1: List Cash Inflows and Outflows



Cash in	Cash out
Jack's salary	Land/house
Joanie's salary	Truck
	Car
	Utilities
	Food
	Day care
	Clothing
	Fuel
	College Fund
	Sheep
	Garden
	Gifts
	Donations



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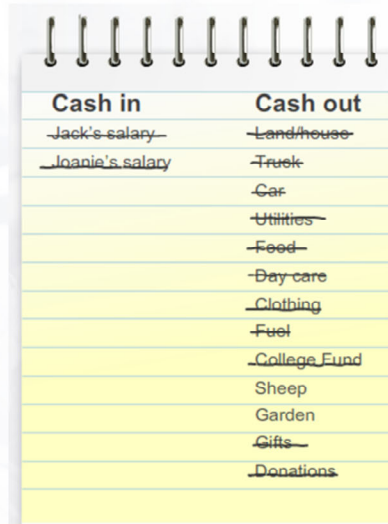
Dad suggests that the best place to start is to list all cash inflows and all cash outflows by category.

The only cash inflows Jack and Joanie have at this time is their take-home pay from their jobs.

Jack and Joanie list their loan payments for the land and trailer house, pickup, boat, and car. They then estimate an average monthly amount for their living costs. Finally, they list those costs incurred irregularly, such as a budget for Christmas presents.



## Step 2: Separate Personal and Business Cash Inflows and Cash Outflows



Cash in	Cash out
<del>-Jack's salary</del>	<del>-Land/house</del>
<del>-Joanie's salary</del>	<del>-Truck</del>
	<del>-Car</del>
	<del>-Utilities</del>
	<del>-Feed</del>
	<del>-Day care</del>
	<del>-Clothing</del>
	<del>-Fuel</del>
	<del>-College Fund</del>
	Sheep
	Garden
	<del>-Gifts</del>
	<del>-Donations</del>



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Dad explains that in order to project the cash flow for the business Jack will need to separate business and personal cash inflows and cash outflows by deleting all personal items.

Jack and Joanie remove their current jobs from the list of cash inflows as Jack's income is not relevant to the business and Joanie's may go away.

Then, they remove the personal cash outflows from their list such as the house payment, gifts, clothing, and food.

### Step 3: Estimate Projected Cash Inflows

	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	TOTAL
<b>Cash Inflows</b>													
Flower Sales													
Livestock Sales													
Livestock Product Sales													
Other													
Total Cash Inflows													



Jack projects that if Joanie plants two acres of flowers she could generate \$20,000 in sales. He estimates flower sales of about \$5,000 in May and \$3,000 in June, July, August, September, and October. Also, there will be \$325 from the sale of two lambs in September and \$48 from the sale of wool in May.

Teaching moment: Using the sample cash flow statement, read the amounts aloud again, and have the class enter the information into their forms.

## Step 4: Estimate Projected Cash Outflows

	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	TOTAL
<b>Cash Outflows</b>													
Seed & Plants													
Fuel & Lube													
Insurance													
Supplies													
Utilities													
Labor													
Storage													
Miscellaneous													
<b>Subtotal</b>													
Total Loan Payments													
<b>Total Cash Outflows</b>													

Jack estimates cash outflows of \$1,000 for seeds and plants in March and April, \$100 in May, and \$500 in July. He expects to spend \$558 for fertilizer in March. Also in March, he anticipates \$400 for equipment repairs and budgets \$90 a month from April through November for ongoing maintenance. Likewise, he budgets \$400 for fuel in March and an additional \$100 each month from April through November. Jack thinks he will need \$500 worth of supplies in March and budgets \$150 for each month the rest of the year. He budgets \$30 in January and September for the water bill. Finally, he projects \$15 per month for the sheep.

Jack budgets \$120 in utility costs during the colder months of November through April and \$50 each month in May through October. He decides to budget \$250 for labor in May and \$100 for flower storage in May as well. He enters \$30 toward his property taxes in February and sales tax of \$56 in May and \$22 in June through October to correspond with his expected sales volume in those months. He adds \$50 in February and \$580 in December for insurance. He budgets \$50 per month in May through August to cover vendors' fees at the local farmers market and an additional \$150 for some advertising in May. Finally he adds \$40 a month for any miscellaneous expenses.

Teaching moment: Using the sample cash flow statement, read the amounts aloud again, and have the class enter the information into their forms.

## Step 5: Calculate Net Cash Flow

	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC	TOTAL
<b>Net Cash Flows</b>													
Accumulated Cash Flows													

The last step is to subtract the projected cash inflows from the projected cash outflows for each month and then for the year.

When calculating monthly totals, remember to carry over any cash deficit or surplus from one month to the next. A negative total reflects a cash deficit for a given month, and a positive total reflects a cash surplus.

Teaching moment: Allow class time to calculate and review with them the completed cash flow statement for Jack and Joanie. There is a finished copy of Jack and Joanie’s Cash Flow Statement available to print on the CD.

**Additional Teaching Moment:**

Ask the class (answers in parentheses):

- In which months did Jack and Joanie predict a cash surplus? (Months with a positive value in the Net Cash Flow)
- In which months did Jack and Joanie predict a cash deficit? (Months with a negative value in the Net Cash Flow)
- According to the projected cash flow statement, would the farm business generate additional cash for the family? (Yes! A positive net cash flow for the year indicates the business will generate a cash surplus).

## Types of Cash Flow Statements

- **Historical cash flow statement**
  - A record of actual data from a past time period
- **Projected cash flow statement**
  - Predicts future cash inflows and outflows based on currently known information
- **Both types are useful to business managers**



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A historical cash flow statement is a record of cash inflows and outflows that occurred in the past.

A projected cash flow statement predicts future cash inflows and outflows based on current information. Both types of cash flow statements can be used for planning and decision-making.

Dad explains that the projected cash flow statement they just created indicates that a small farming business would generate additional cash, but not enough to replace Joanie's income. He recommends that if she and Jack start the business, they create and maintain historical cash flow statements so they can compare actual to projected cash inflows and outflows.

## Challenges and Benefits

- **Challenges:**

- Developing, monitoring, and revising takes time and effort
- Market prices, production costs, interest rates, and capital expenditures can be difficult to project



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Developing and monitoring cash flow statements presents both challenges and benefits to a business. Review the challenges listed on the screen.

## Challenges and Benefits *(cont.)*

- **Benefits:**

- Provide a basis for better projections of cash inflows and outflows
- Reveal loan repayment capacity
- Can be used to plan the timing of purchases and payments
- Help managers identify the impact of unexpected fluctuations in inflows and outflows
- Over time, help managers become better at projecting inflows and outflows and avoiding unexpected negative fluctuations



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Developing and monitoring cash flow statements presents both challenges and benefits to a business. Review the benefits listed on the screen.

## Quiz Time!

**Which of the following are uses for a cash flow statement?**

1. Reveals loan repayment capacity
2. Lists the cash inflows and outflows of a business over time
3. Determines the net worth of a business
4. Estimates business profitability



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The next few slides contain quiz questions for the class. Allow for responses.

Answer:

1 and 2



## Quiz Time!

**What is the proper order of the steps listed below?**

- List all cash outflows in the months they occur
- List all cash inflows in the months they occur
- Subtract cash inflows from cash outflows for each month and then for the year
- Make a list of all sources of cash inflows and outflows
- Separate personal from business cash inflows and cash outflows



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The next few slides contain quiz questions for the class. Allow for responses.

Answer:

The bullets are listed in this step order: 4, 3, 5, 1, 2

## Quiz Time!

**Which types of cash flow statements should a farm manager develop, monitor, and analyze?**

1. A projected cash flow statement
2. A historical cash flow statement
3. Both a projected cash flow statement and a historical cash flow statement
4. Neither, cash flow statements are for lenders only



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The next few slides contain quiz questions for the class. Allow for responses.

Answer:

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## Homework

- **Create a projected cash flow budget for your business**
- **Then create a historical cash flow statement and track actual cash inflows and outflows**
- **Compare your projections to your historical performance**



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You have finished Session One!

Review the Homework on the screen, providing instruction for how the class can find the Cash Flow Statement Template and Instructions on the CD.

Allow for review debrief and any additional questions.