

Effective financial statements with the RD Financial Tool from RightRisk.org

These are very uncertain times. Everyone involved in production agriculture is keenly aware of the reasons.

Now, more than ever, having your financial profile in order is important. Constructing and properly interpreting financial statements should be a top priority.

Assembling a comprehensive picture of your financial health is an integral part of risk management planning and allows a better understanding of what a lender considers when evaluating your operation's creditworthiness. You are also better prepared to measure a business' financial position and overall performance as well as manage for success.

THE RD FINANCIAL TOOL

RD Financial is an interactive, spreadsheet-based risk analysis tool that can help construct financial statements, show the interaction of those statements, calculate the resulting financial ratios, and help evaluate a farm or ranch's financial performance. The tool generates the four fundamental financial statements: income statement, cash flow statement, balance sheet, and owner equity statement (see Figure A). It calculates financial ratios based on the data entered and contains help functions and allows users to save information or reset and start over. For a detailed presentation on the RD Financial Tool, select "Tool Support" from the opening menu.

MULTI-ENTERPRISE FARM EXAMPLE

The RD Financial Tool has a built-in example farm to highlight its use. Entering the necessary financial data is the first step in using the RD Financial Tool. This includes completing the sections for crop revenue and expenses, livestock revenue and expenses, taxes and insurance, assets and liabilities, and miscellaneous and overhead where appropriate. Crop expenses are divided by enterprise, and the tool includes multiple extra spaces for users to enter other expenses not listed in the example.

The tool was designed to help users see and better understand the interaction of the information across the financial statements and associated ratios and find any discrepancies in the information entered.

RATIOS AND ANALYSIS

RD Financial generates a set of 16 financial ratios based on the financial statements. These ratios are divided into five categories and are commonly used by lenders to evaluate a borrower's financial situation: liquidity, solvency, profitability, repayment capacity, and financial efficiency (see Figure B).

To see a detailed explanation of each ratio, simply click the "Off/On" button next to each ratio. The tool generates a thermometer (red/yellow/green) for each ratio based on industry standards to indicate ratio status (critical/caution/healthy).

The RD Financial Tool also includes an example credit scoring section and offers an explanation of how a lender might estimate creditworthiness for operating and term loans. The tool relies on four ratios with a score for each ranging from one to five (excellent to high risk) in the operating loan example. This feature can provide users a method to identify and address problem financial areas in their business before meeting with potential lenders.

James Sedman is a consultant to the Department of Agricultural and Applied Economics in the University of Wyoming College of Agriculture and Natural Resources, and **John Hewlett** is a farm and ranch management specialist in the department. Hewlett may be reached at (307) 766-2166 or hewlett@uwyo.edu.

Figure A

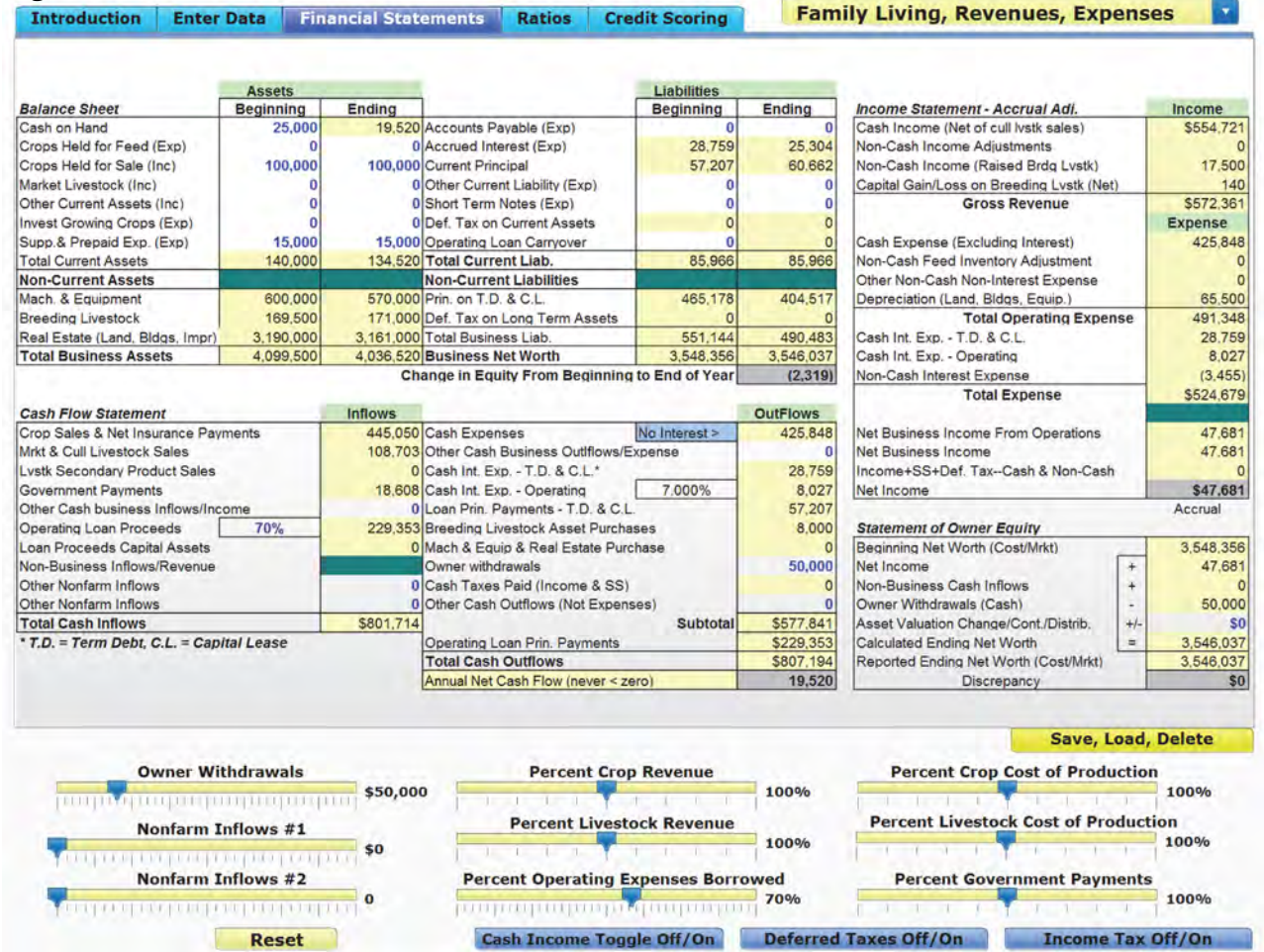
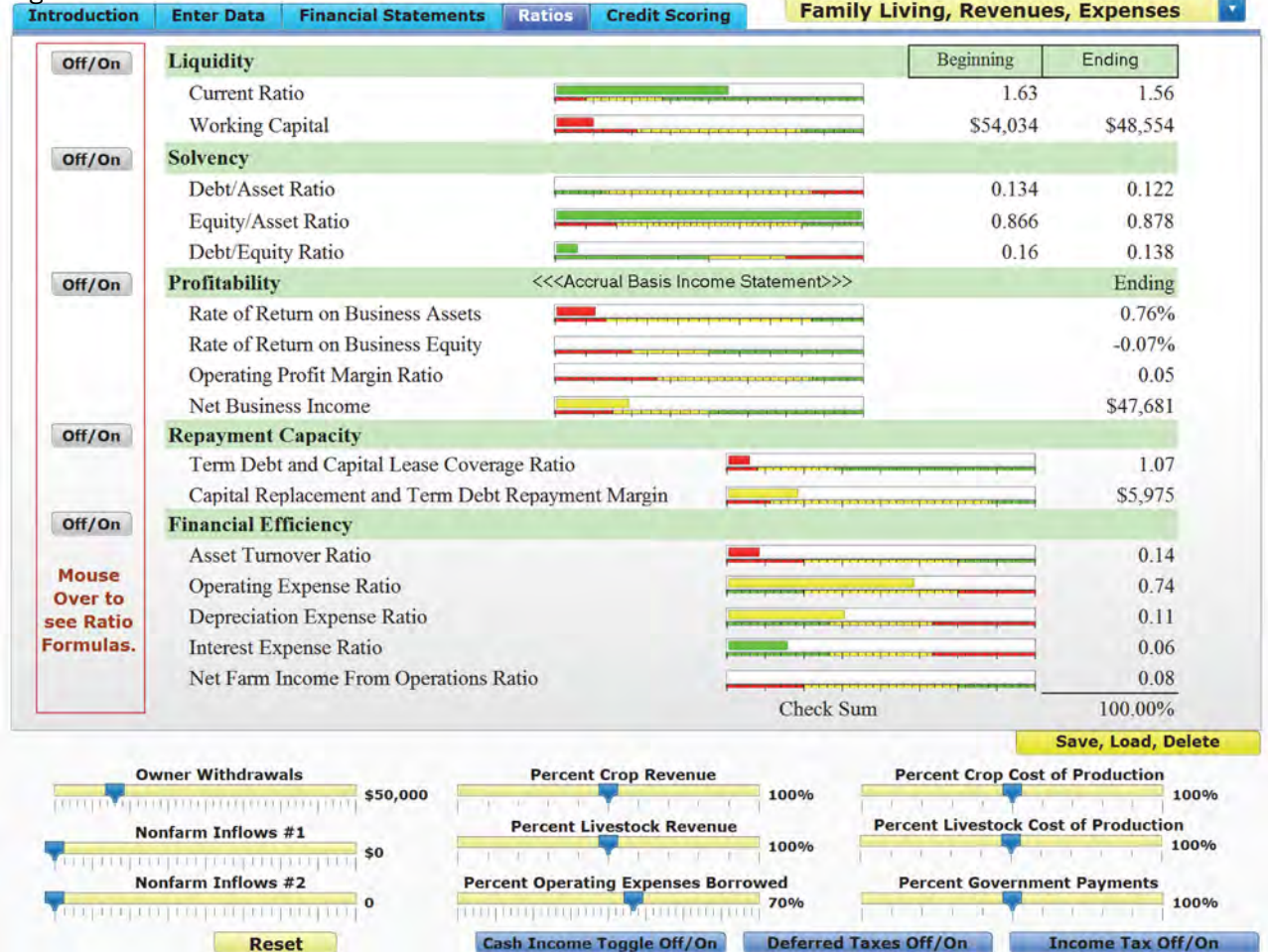


Figure B



FOR MORE INFORMATION

RD Financial is a risk analytics tool included in the RightRisk Analytics Toolbox. Visit RightRisk.org and select Risk Management Tools from the Resources menu to download. RightRisk.org is a premier risk management site designed to assist managers with risk management planning and analysis. Numerous courses, risk management profiles, and other resources, in addition to the RightRisk Analytics toolbox, may be found at the site.

IMPORTANT REMINDERS

- **Spring crop insurance signup deadline—March 15**
- **Payroll Protection Program (PPP) loans are now available to ag producers. Contact your bank for more details.**
- **ARC/PLC election due—March 1.**
- **A third round of CFAP payments is coming soon.**