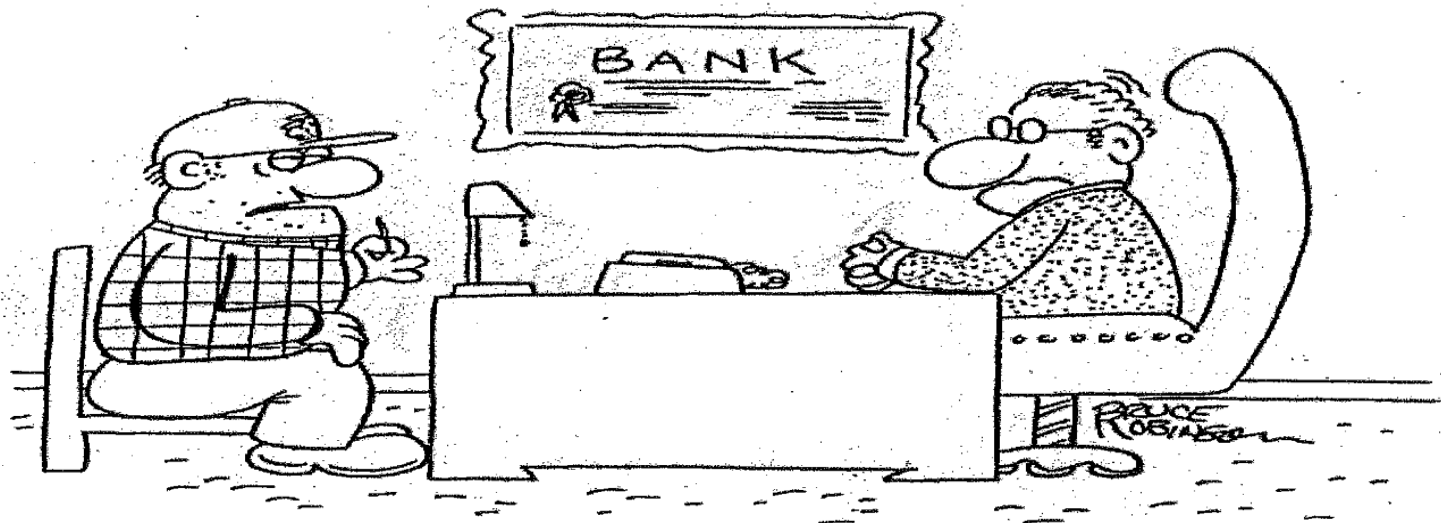




FARMER AC

*Don't buy it, if you can lease it.
Don't lease it, if you can rent it.
Don't rent it, if you can steal it!*

*Curt Covington, Sr. Vice President
Farmer Mac, Washington DC*



**“Sometimes it’s hard to figure who’s dumber
— me for borrowing or you for lending.”**

Why The Title?

I Wanted Your Attention

Think Strategically About Your Financial
Decisions

Remaining Nimble in a Volatile Business



Keys To Cash Flow Freedom

#1

Commit to Short Term Planning

#2

Know Your Cost Structure

#3

Control Your Cost Structure



Commit to Planning

Remove the Apprehension

Find the Value

Force Yourself to Revisit Regularly

Get Better at it



Know Your Cost Structure

How Do You Manage Your Kids?
By Managing Their Behavior!

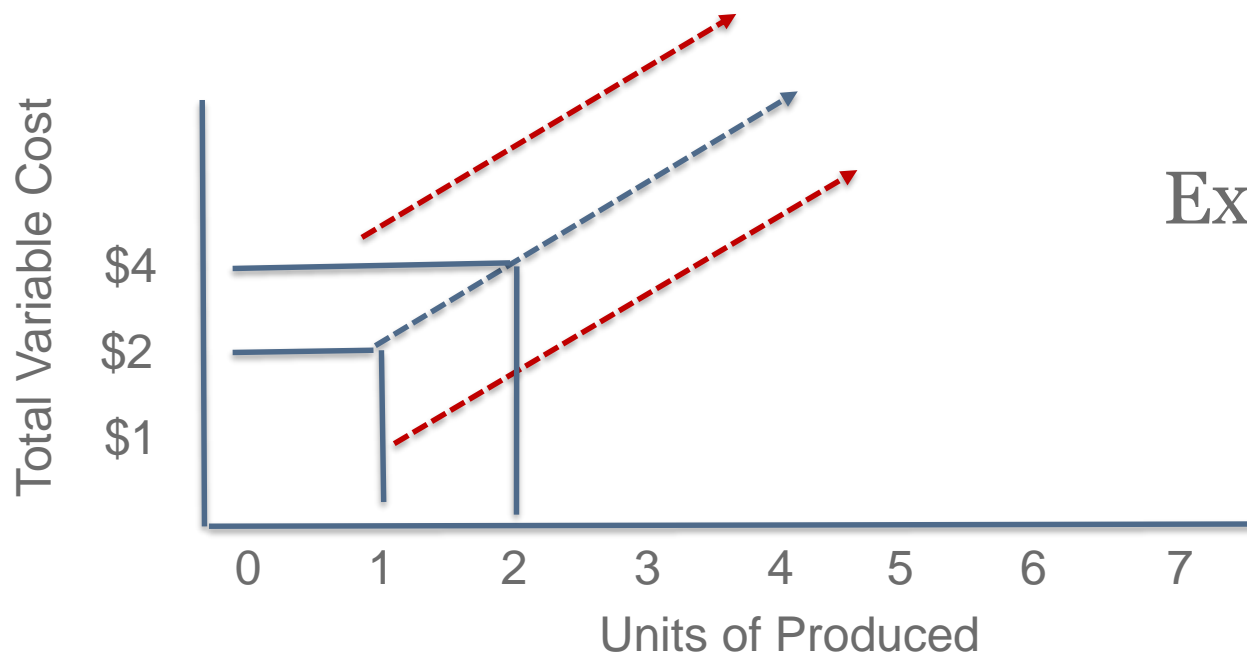
Same Goes For Costs!



Know Your Cost Structure

Costs can be separated into *Variable* and *Fixed* components for short run planning

Variable Costs – Those cost that change in direct proportion to changes in activity



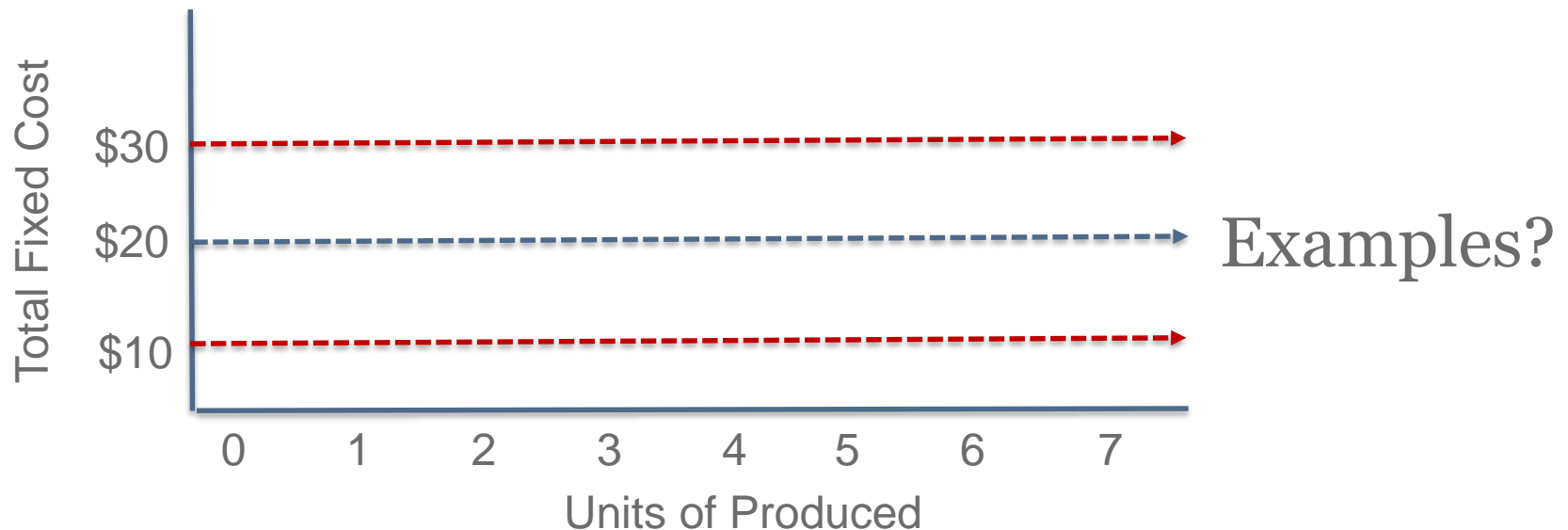
Examples?



Know Your Cost Structure

Costs can be separated into Variable and Fixed Components

Fixed Costs – Those cost that do not change in the current operating period regardless of the changes in activity



Know Your Cost Structure

Let's Take a Look at the Following Hypothetical
2018 Projected Income Statement for Top
Producer Farms



Know Your Cost Structure

Top Producer Farms 2018 Projected Income Statement

		<u>Per Unit</u>	<u>% of Revenue</u>
Number of Units Sold	250		
Farm Revenue	\$ 100,000	\$ 400	100%
Variable Costs	50,000	200	50%
Contribution Margin	\$ 50,000	\$ 200	50%
Fixed Costs	30,000	120	30%
Net Farm Profit	\$ 20,000	\$ 80	20%

Notice:

Costs are Divided into Variable vs Fixed “Behaviors”

New Term: “Contribution Margin/Contribution Margin Per Unit”

“Per Unit” and “% of Revenue” are based on “Units Sold” not Acres farmed



Know Your Cost Structure

Top Producer Farms 2018 Projected Income Statement

		<u>Per Unit</u>	<u>% of Revenue</u>
Number of Units Sold	250		
Farm Revenue	\$ 100,000	\$ 400	100%
Variable Costs	50,000	200	50%
Contribution Margin	\$ 50,000	\$ 200	50%
Fixed Costs	30,000	120	30%
Net Farm Profit	\$ 20,000	\$ 80	20%

Notice:

A New Term: “Contribution Margin %”

Key Takeaway Last Two Slides:

“Net Farm Profit” and Farm Revenue DO NOT Move in Tandem



Rule #2: Control Your Costs

Learn to Control (Manage) Cost (and Cash Flow) in 3 Easy Steps

- 1) Calculate Operating Breakeven Points
- 2) Calculate Degree of Leverage
- 3) Scenario Building (What If's?)



Calculating Your Operating Breakeven Points

Breakeven Point in Units = The number of units produced and sold needed to cover all variable and fixed costs and produce a net farm profit of zero.



Calculating Your Breakeven Points

Breakeven Point in Units Sold Defined:

Total Fixed Costs divided by CM Per Unit

Top Producer Farms
2018 Projected Income Statement

		<u>Per Unit</u>	<u>% of Revenue</u>
Number of Units Sold	250		
Farm Revenue	\$ 100,000	\$ 400	100%
Variable Costs	50,000	200	50%
Contribution Margin ("CM")	\$ 50,000	\$ 200	50%
Fixed Costs	30,000	120	30%
Net Farm Profit	\$ 20,000	\$ 80	20%

Breakeven Point in Units

150 [FC *divided by* CM PER UNIT]



Understand this and you are on your way to managing Cash Flow From Operations

Calculating Your Operating Breakeven Points

Breakeven Point in Revenue = The Farm Revenue needed to cover all variable and fixed costs and produce a net farm profit of zero.



Calculating Your Breakeven Points

Breakeven Point in Farm Revenue Defined:

Total Fixed Costs divided by CM Percentage

Top Producer Farms
2018 Projected Income Statement

		<u>Per Unit</u>	<u>% of Revenue</u>
Number of Units Sold	450		
Farm Revenue	\$ 100,000	\$ 400	100%
Variable Costs	50,000	200	50%
Contribution Margin (CM)	\$ 50,000	\$ 200	50%
Fixed Costs	30,000	120	30%
Net Farm Profit	\$ 20,000	\$ 80	20%

Breakeven Point in Revenue

\$

60,000

[FC divided by CM PERCENTAGE]



Degree of Operating Leverage

Degree of Operating Leverage = an efficiency ratio that measures the rate at which net farm profit changes in relation to changes in farm revenue. Remember they do not move in tandem.

Companies with higher fixed costs compared with variable costs are considered to have more leverage because the higher fixed costs require more production in order to break even.



Calculate Degree of Operating Leverage

Degree of Operating Leverage Defined:

Contribution Margin divided by Net Farm Profit

Top Producer Farms
2018 Projected Income Statement

		Per Unit	% of Revenue
Number of Units Sold	250		
Farm Revenue	\$ 100,000	\$ 400	100%
Variable Costs	50,000	200	50%
Contribution Margin ("CM")	\$ 50,000	\$ 200	50%
Fixed Costs	30,000	120	30%
Net Farm Profit	\$ 20,000	\$ 80	20%

Degree of Operating Leverage

2.50

[CM divided by NET FARM PROFIT]

Operating Leverage Can Build or Bury a Business Over Time. Understand this and you are on your way to managing Cash Flow From Operations



Scenario Building

A series of “what ifs” that allow the top producer to see the effects of changes in various components of the Projected Income Statement.

Take our Base Case below and start building good and bad scenarios

Top Producer Farms 2018 Projected Income Statement

		<u>Per Unit</u>	<u>% of Revenue</u>
Number of Units Sold	250		
Farm Revenue	\$ 100,000	\$ 400	100%
Variable Costs	50,000	200	50%
Contribution Margin ("CM")	\$ 50,000	\$ 200	50%
Fixed Costs	30,000	120	30%
Net Farm Profit	\$ 20,000	\$ 80	20%



Scenario Building

What if we thought that Revenue Per Unit increased by 10% from our base projections AND assuming everything else remains unchanged

Top Producer Farms 2018 Projected Income Statement

		<u>Per Unit</u>	<u>% of Revenue</u>
Number of Units Sold	250		
Farm Revenue	\$ 110,000	\$ 440	100%
Variable Costs	50,000	200	45%
Contribution Margin ("CM")	\$ 60,000	\$ 240	55%
Fixed Costs	30,000	120	27%
Net Farm Profit	\$ 30,000	\$ 120	27%

\$400 + \$40
10%

Increased by 50%
(\$10 / \$20 = 50%)

	<u>Before</u>	<u>After</u>	<u>Change</u>
Breakeven Point in Units	150	125	(25)
Breakeven Point in Revenue	\$ 60,000	\$ 55,000	\$ (5,000)
Degree of Operating Leverage	2.50	2.00	(0.50)



Scenario Building

What if we thought that Revenue Per Unit declined 10% from our base projections AND assuming everything else remains unchanged

Top Producer Farms 2018 Projected Income Statement

		<u>Per Unit</u>	<u>% of Revenue</u>
Number of Units Sold	250		
Farm Revenue	\$ 90,000	\$ 360	100%
Variable Costs	50,000	200	56%
Contribution Margin ("CM")	\$ 40,000	\$ 160	44%
Fixed Costs	30,000	120	33%
Net Farm Profit	10,000	\$ 40	11%

\$400 - \$40
-10%

Decreased by 50%
(\$10 / \$20 = 50%)

	<u>Before</u>	<u>After</u>	<u>Change</u>
Breakeven Point in Units	150	188	38
Breakeven Point in Revenue	\$ 60,000	\$ 67,500	\$ 7,500
Degree of Operating Leverage	2.50	4.00	1.50



Scenario Building

What if a slick sales person says “ my fertilizer will cost you an additional “\$10” per unit but guaranteed to increase your yield by “25 units”

Top Producer Farms 2018 Projected Income Statement		<u>Per Unit</u>		<u>% of Revenue</u>
Number of Units Sold	275			
Farm Revenue	\$ 110,000	\$ 400		100%
Variable Costs	57,750	210		53%
Contribution Margin ("CM")	\$ 52,250	\$ 190		48%
Fixed Costs	30,000	109		27%
Net Farm Profit	22,250	\$ 81		20%
	<u>Before</u>	<u>After</u>		<u>Change</u>
Breakeven Point in Units	150	158		8
Breakeven Point in Revenue	\$ 60,000	\$ 63,158	\$	3,158
Degree of Operating Leverage	2.50	2.35		(0.15)

250 + 25

\$200 + \$10

Impact



Ok Let's Blow Your Mind.....

Target Breakeven Point in Units Defined:

Fixed Cost + "Desired Net Profit" divided by Contribution Margin Per Unit

Target Breakeven Point in Farm Revenue Defined:

Fixed Cost + "Desired Net Profit" divided by Contribution Margin Percentage

Top Producer Farms

2018 Projected Income Statement

		<u>Per Unit</u>	<u>% of Revenue</u>
Number of Units Sold	250		
Farm Revenue	\$ 100,000	\$ 400	100%
Variable Costs	<u>50,000</u>	<u>200</u>	<u>50%</u>
Contribution Margin ("CM")	\$ 50,000	\$ 200	50%
Fixed Costs	<u>30,000</u>	<u>120</u>	<u>30%</u>
Net Farm Profit	\$ 20,000	\$ 80	20%



Ok Let's Blow Your Mind.....

Target Breakeven Point in Units Defined:

Fixed Cost + “Desired Net Profit” divided by CM Per Unit

$$(\$30,000 + \$25,000) / \$200 = 275 \text{ Units Sold}$$

Target Breakeven Point in Farm Revenue Defined:

Fixed Cost + “Desired Net Profit” divided by CM Percentage

$$(\$30,000 + \$25,000) / .50 = \$110,000$$



Wrap Up

Make the Time and Make the Effort to Plan

Knowing Your Cost Structure is Powerful

Manage Your Cost and You Manage Your
Operating Cash Flow

Operating Leverage (Fixed Costs) Can Make or
Break a Business





Thank You

Questions?