16 Making Money
Resource Kit for Nova Scotia Farmers

How Will You Know if Your Operation is Making Money?

Cash Flow, Net Worth and Profit – These are the three pillars that sustain a business. All need to be positive for a business to thrive in the long run.

Cash flow tracks the cash dollars into and out of the farm business. You should be able to balance all of the money that came in and went out:
start up money + cash from operations + borrowed money = cash paid on expenses + debt payments + end of year money.
In horticultural operations, cash flow expenses will be high in the spring as crops are planted and income will be high in the fall when crops are sold. Therefore, cash flow requires planning and savings to be sure income covers future costs. Cash flow records are a way to keep track of your money, ensure that you can cover monthly expenses, and are crucial to long term profitability

Net worth tracks your investments in the farm. It is also called the **balance sheet**.

Net worth = everything the business OWNS minus everything it OWES

Assets You Manage – What you Owe = Your Ownership

Assets – Liability = **Equity**

Some assets tend to go up in value over time, such as land. This is called appreciation. Some assets go down in value over time, such as equipment. This is called depreciation. Depreciation is a measure of the wear, tear, and obsolescence of an investment. The primary function of net worth calculations is to measure the risk-bearing ability or financial solvency of your business or, in simple terms, how much you really own versus how much the bank owns.

Profitability is measured with the Income Statement. It is the result of your operation's work, decisions, and return on investment.

Value of Production – Cost of Production = Profit

Profitability is harder to track as it blends cash flow and investment decisions. It also makes adjustments for family withdrawals, “free or family” labor, and return on investment.

Some examples of good cash flow, but low profitability:

- Living off of inventories or depreciation, and not reinvesting in the operation.
- Outside income or off farm jobs that help reduce need for family living withdrawals.
- Borrowing money.
- Not paying bills.

Some examples of bad cash flow, but good profitability:

- An expanding business with increasing assets, but few cash sales.
- High withdrawals for family living, for example, college expenses.
- Paying down debt rapidly.
- Buying next year’s assets from this year’s cash (prepay for fertilizer, etc.).
- Increase in accounts receivable (amount of money you are owed for products that were sold).

For your tax return you may want to use cash accounting, but for profitability you want to use accrual accounting. Accrual accounting looks at changes in inventory and price; changes in accounts payable and receivable, appreciation and depreciation, unpaid labor, opportunity costs to work elsewhere, interest on equity, and your labor and management inputs.

Interest on Equity

- Can you borrow money without paying interest?
- Do you have an “opportunity” to put your money somewhere else?
- Do you want to earn interest/dividends on your money in the stock market?
- Shouldn’t you earn interest on the money invested in your farm?
- Plan to pay yourself 3% minimum on your equity invested in the farm!!

Value of Labor and Management

What is the value of your efforts on the farm? What is the “opportunity” for you to work elsewhere? A simple charge for your efforts will help you find a value to evaluate your business. What could you earn if you worked elsewhere in a similar job?

What Does a Manager Do?

Mangers make the decisions about investments and tasks. They define the mission and philosophy for the operation. They develop the plan, hire and motivate the people to implement the plan, invest in the assets to implement the plan, set priorities, and evaluate the results so they can adjust the plan if needed.

Partial Budgeting

This helps make decisions for smaller investments that do not affect whole farm operation. Look at the expected increases to income and decreases to expenses for a project, compared to decreases in income and increases in expenses. This will help you decide how much you can invest and the impacts on other parts of the business.

If You Can't Measure it, You Can't Manage it!

- Numbers, Numbers, Numbers!
- Count, measure, quantify, allocate
- Establish controls, set goals
- Productivity must be quantifiable – only way to measure productivity

[Note: The content for this fact sheet was taken from the *Guide to Farming in NY: What Every Ag Entrepreneur Needs to Know*, a publication of the NY Beginning Farmer Project, Cornell Small Farms Program and reviewed by Lori Kittilsen, Business Development Specialist, Nova Scotia Department of Agriculture, March 2010.]

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