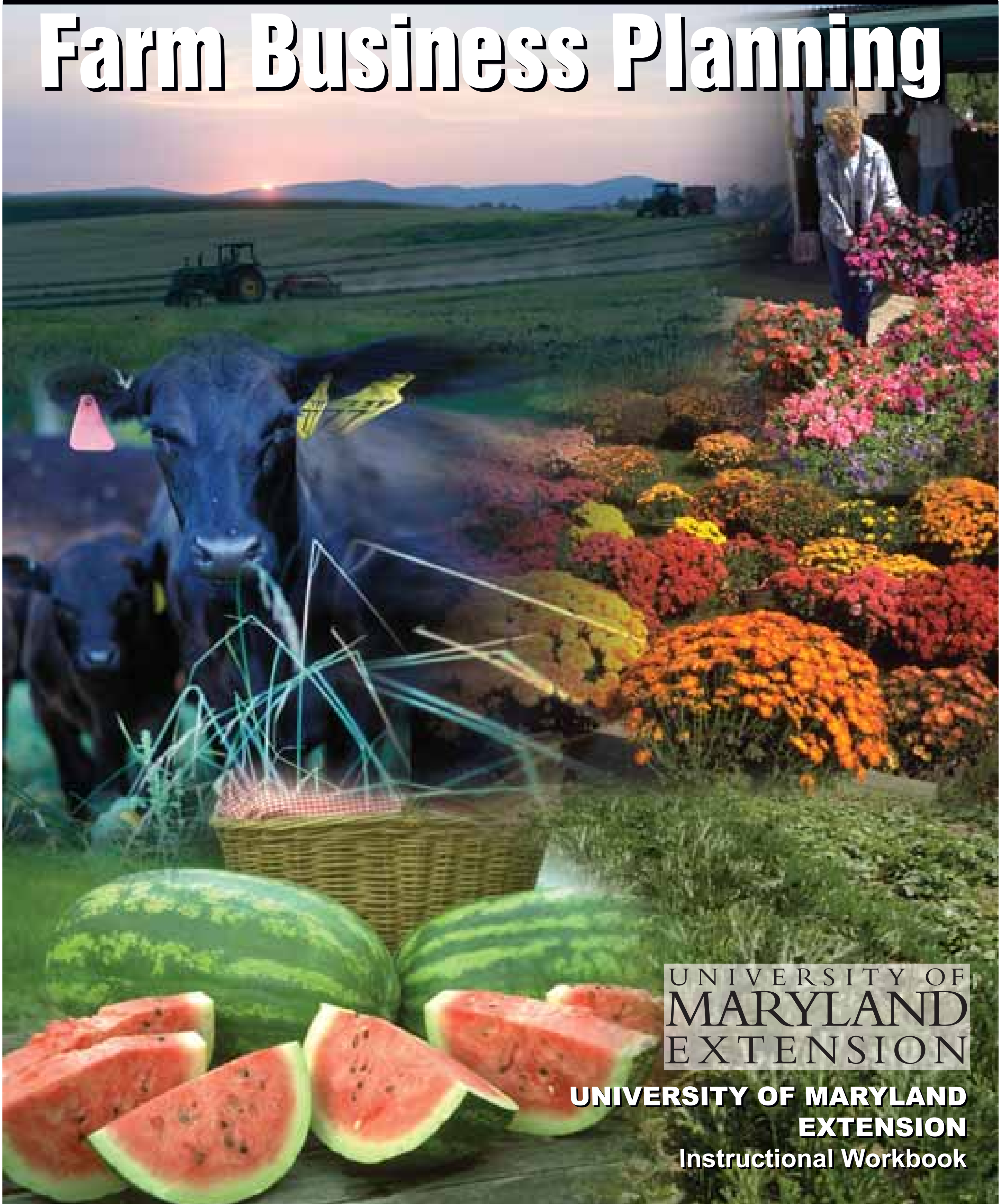
Farm Business Planning



UNIVERSITY OF MARYLAND EXTENSION

Instructional Workbook

UNIVERSITY OF
MARYLAND
EXTENSION

Farm Business Planning

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FORWARD

Planning is essential to any business, no matter how large or small the inventory, payroll, and bank account. To be successful, farm operaters must know their current position and future plans. Thinking about your plans is not enough! Taking time to formulate ideas, evaluate your business, devise a strategy, and anticipate possible problems will help your business be succesful.

This workbook was designed so that the thoughts and objectives for your business can be organized and thoroughly documented. In the long run, your business plan will serve many purposes, such as:

- Defining a new business
- Setting goals and planning steps to achieve them
- Evaluating the effectiveness of business and marketing strategies
- Setting a direction for the business for the next five years
- Planning, growth and development for established businesses
- Supporting a loan application

A good business plan should be realistic, simple, specific, and complete.

- ✓ Is your plan realistic? Are your goals and dates realistic for your farm operation?
- ✓ Is your plan simple? Can you and others read and understand the farm business plan?
- ✓ Is your plan specific? Are your goals and objectives measurable?
- ✓ Is your plan complete? Does it include all aspects of your farm business?

HOW TO USE THIS WORKBOOK

Write your plan so that anyone can easily read and understand it. The business plan may be used to communicate to partners, employees or others who are directly involved in the business. Lenders and financial institutions who may not be familiar with agricultural terms and farm production may also read your plan. Make the plan easy for other audiences to understand.

There are various ways to use this workbook. You can develop your business plan simply by filling out the pages. If you use this method, you will find that most of the sections are useful in helping you plan your business. Leave the sections blank that don't apply to your business.

You may use this workbook as a guide for developing an electronic version of the business plan. This is a better method if you find that the space allotted is too small or too large. An electronic version is also easier to update. Business planning tools, including a business plan template, spreadsheets, case studies and business assessment tools are available at the Maryland Rural Enterprise Development Center www.extension.umd.edu/MREDC.

In order to develop a good business plan, you will need to gather information to organize it into a concise summary. Some needed information is:

- Personal or Household Budget – what are your family income and expenses?
- Production Timeline – calendar planting and harvesting dates or breeding and sales dates so you have a clear picture of labor, expenses and income decisions.
- Production Records – these are needed for many purposes on the farm so keep very clear and concise production records.
- Financial Records – any financial records you have such as tax records, loan information etc. will be beneficial in completing your business plan.
- Contact List – these are friends, family and/or professionals that you trust and value for their expertise, advice and opinion. The farming and business community is a very strong network of talented individuals that can help your business succeed.

And remember, the planning process is never complete. Continue to use, review, and analyze the plan as your operation grows and changes. The end of the calendar year is always a great time to review it.

EXECUTIVE SUMMARY

While the Executive Summary is located in the front of the document, it is the last task in writing a business plan. Write the summary when the workbook is finished. It is an overall summary of your business goals and objectives and how you plan to meet them in the next five years.

MISSION STATEMENT

A mission statement succinctly defines your business. It describes what you are trying to accomplish and what you value. It explains "who we are, what we do, where we're headed". A mission statement gives you a clear direction for the future and should motivate and compel you. It is the foundation upon which you operate your business.

A good mission statement should clearly answer:

- ✓ Why does your business exist?
- ✓ What purpose does your business serve?
- ✓ Where is your business headed?

Mission statements must reveal more than a motive of profit.They should contain values, activities and the identity of the farm. Write your statement in a short paragraph with enough detail to provide a clear direction while still being flexible. A mission statement is like a book cover. It provides the reader with a glimpse of the story which lies ahead.

GOALS

Businesses must plan for change and growth by setting goals. Effective goals have five characteristics. They should be SMART--specific, measurable, attainable, rewarding and time bound. If you set SMART goals, you have a better chance of accomplishing them. Your business plan will have short-term and long-term goals. Short-term goals are accomplished in less than a year. Long-term goals take a year or longer to accomplish. List your long-term goals in the mission statement. These are incorporated into other sections of the business plan.

SMART Goals are:

Specific
Measurable
Attainable
Rewarding
Time Bound

A business's goals can include:

- Production (yields, quality, efficiency)
- Marketing (sales, distribution, percent market share, advertising)
- Financial (profit, net worth, cash flow, cost per unit of output)
- Legal (estate, land preservation)
- Personnel (management, employee retainment, hiring, skills)

MISSION STATEMENT

HINT: *Mission and goal statements can be good marketing strategies for advertising and promotional pieces.*

GOALS

Short Term

Long Term

BACKGROUND INFORMATION

Business Name and Address:

Email Address: Website Address:

Telephone:

Business: Mobile:

Home: Fax:

Type of Ownership: ☐ Sole Proprietorship ☐ Limited Liability Co.

☐ Partnership ☐ Cooperation ☐ Other

Business Advisors:

Accountant	Attorney
Name:	Name:
Address:	Address:
City, St, Zip:	City, St, Zip:
Phone:	Phone:
Bank	**Insurance Agent**
Name:	Name:
Address:	Address:
City, St, Zip:	City, St, Zip:
Phone:	Phone:
Extension Agent	**Other (crop/livestock advisor etc.)**
Name:	Name:
Address:	Address:
City, St, Zip:	City, St, Zip:
Phone:	Phone:

Who is Involved in the Operation?

Name:	Position:
Name:	Position:
Name:	Position:
Name:	Position:
Name:	Position:

History and Overview of the Business

This is approximately one page on the history of the operation and a summary of current activities. This information is helpful to have in the business plan so the reader understands the past and present farm operation.

Some questions that should be addressed include:

- Where is the operation located?
- How and when did the operation begin?
- How is the farm currently operating?
- What is the general productivity, management, and situation of the farm?
- What are general practices of the operation? (i.e., conservation, environmental, tillage, marketing, risk)

Operation Layout

Provide a brief summary of the operation's layout. Aerial photos or maps can be included in the appendix to show location and fields.

History and Overview of the Business

Contracts, Permits, Certifications and other Legal Obligations

This part of the business plan lists the farm and owners' legal and contractual obligations (verbal and/or written). Contracts include mortgages, marketing agreements, land leases, and federal programs such as CREP, WHIP or EQIP (equipment, land, etc. will be listed with resources). Depending on the products and services sold, you may be required to get permits and/or certifications (planning & zoning, health department, food handling, processing, marketing). Discuss areas where the farm is in a good position and where improvements can be made. Be as detailed as you can.

Insurance

List any insurance policies on the farm, crops, health, life, home, liability, and auto.

Estate Plan/Will

Provide a brief summary of your farm transition plans and how property and assets will be divided. This summary is not intended to take the place of an estate plan. You should have a separate and detailed transition and estate plan for the farm.

Retirement

What are your retirement options and plans? Consider savings, Medicare, social security, IRA, and others.

Conservation/Environmental

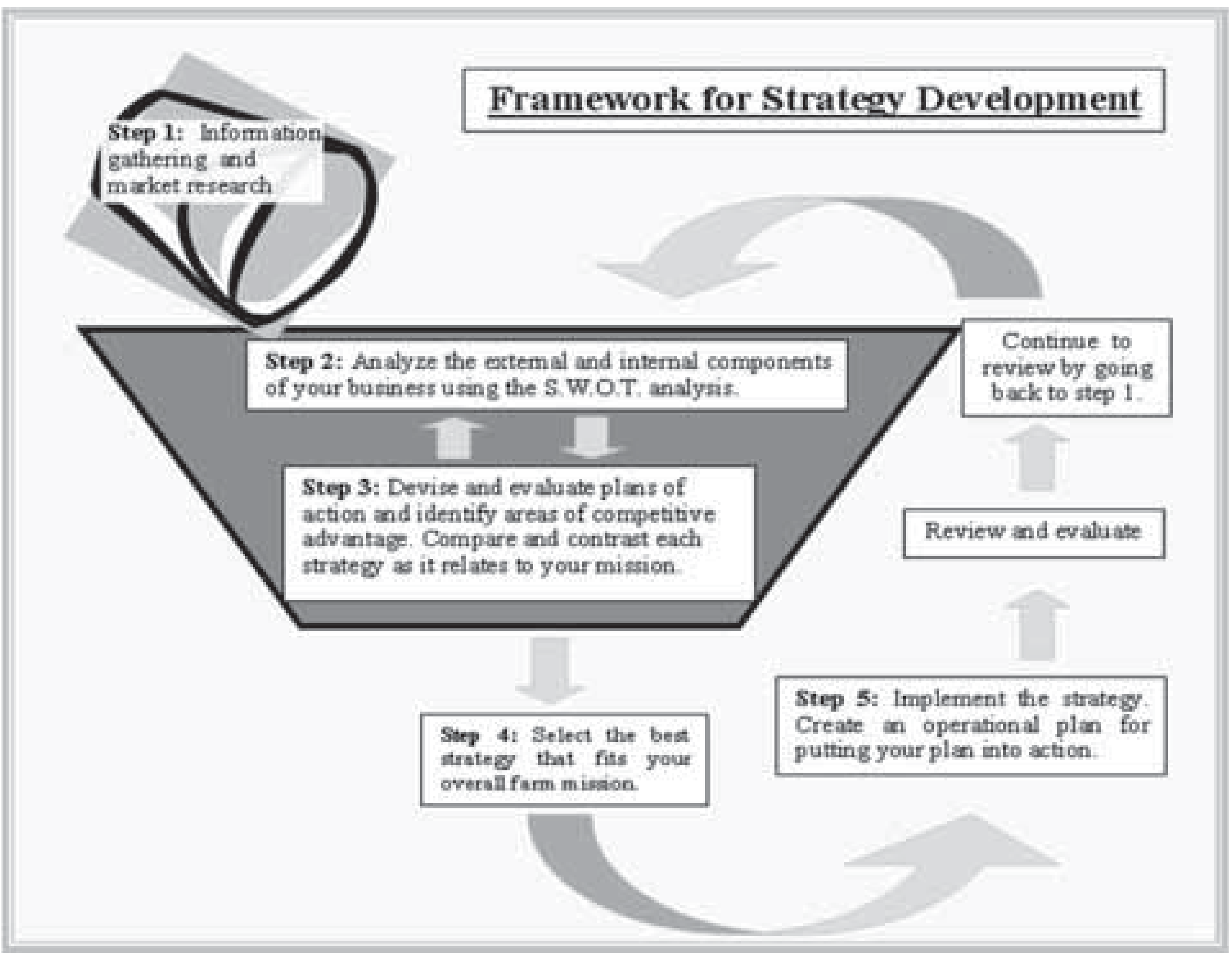
Best Management Practices on the farm for conservation, water quality and the environment are essential on today's farm. Include a list of conservation plans, nutrient management and tillage practices in the appendix.

FORMULATE A FARM STRATEGY

Developing an overall farm strategy is an important component of business development. The strategy includes steps focused on market segments and their attributes and forming a strategy based on the needs of each segment. Formulating a strategy is an ongoing process of discovery and creativity. Strategy formulation is not easy, but it does not have to be hard either.

Developing a strategy is a series of steps:

Step 1: Gathering information and conducting market research.
Step 2: Analyzing the external and internal components of your business using the S.W.O.T. analysis.
Step 3: Creating plans of action and identifying areas of competitive advantage.
Step 4: Selecting the best plan that fits your overall farm mission.
Step 5: Implementing and evaluating the strategy.



Step 1: Information gathering and market research

Some farmers already know exactly what they want to do, how they are going to do it, and why they want to do it. However, many farmers never take the time to consider what the *customer* wants, why the *customer* wants it or how the *customer* wants it. Many of these same farms never consider why their products or services would be sought after more than their competitors would. The notion of creating and maintaining a "competitive advantage" is a key component of the strategy formulation. It is no surprise that information gathering and market research are the first components of strategy building.

Market Research - Research your current and potential markets to identify trends, competitors, needs and buyers. Be sure to take time to collect data. Obtaining good data serves as the foundation for formulating an effective strategy. The better the information, more strategic your plan will be.

Never rely only on your opinion of what the market wants. There are a number of tools that you should consider for your research:

- *Networking:* A one-on-one interview can help generate ideas. Do not forget to interview other business owners or operators who may be able to provide good information on what has or has not worked for them. Be sure to talk with similar farms and producers. Attending tradeshows, conferences and business functions may provide an opportunity to meet, talk, and network about market trends. Sales representatives also are good sources of information.

- *Demographics:* Information about the consumers in your area can be very helpful in marketing to them. The U.S. Census and Small Business Administration are great places to find this information.

- *Observation:* Simply taking time to observe can be a powerful tool. What are people buying? What are competitors offering?

- *Surveys:* Surveys can be written or oral. You can distribute a written survey to a wide range of the population. Consider using an incentive, such as free products or coupons to increase the survey response rate.

- *Focus Groups:* Identifying a small group of potential consumers and asking specific questions about the product/service can provide detailed information.

List what type of market research tools you plan to use:

List the results of market research, including webpages and social media sites. Markets change so it is important to include the source and date of information.

Industry Trends and Analysis: In the space below, identify the major trends in the industry. Start with a broad overview and then specifically identify trends that are significant to your product or service.

HINT: Trade journals, census information, government studies, traffic surveys and professional data sources can be helpful.

List key industry trends here:

Step 2: S.W.O.T. analysis

S.W.O.T. analysis is an analytical tool used to collect information and guide the decision making process in order to obtain strategic advantages.

S.W.O.T. is an acronym for:

- **S**trengths
- **W**eaknesses
- **O**pportunities
- **T**hreats

Strengths and Weaknesses - Evaluation of the Internal Environment

The strengths and weaknesses section is internal to your business and provides insight into what components are available to provide competitive advantages. When developing a strategic plan, the competitive advantages will be a key determinant of profitability.

Identifying weaknesses allows you to develop methods for improvement and set priorities based on future organizational direction. Examples of weaknesses include: *internal operating problems, inexperience, lack of infrastructure, low worker productivity, old or obsolete technology, worn equipment and facilities, poor financial situation, bad community reputation, or inadequate leadership capacity*.

The factors above also may be sources of strengths for the organization. Examples of strengths include: *excellent operating efficiency, high worker productivity, leading-edge technology, good financial standing, high industry reputation, excellent brand image and effective leadership capacity*.

The internal strengths and weaknesses allow business owners to acknowledge the factors needed to build on or exploit to gain a competitive edge in the external environment. Be open and honest with yourself about your operation.

Areas for exploration include:

- Financial Resources
- Management Capability
- Infrastructure
- Land Capacity
- Location

List the internal strengths of the farm business.

List the internal weaknesses of the farm business.

HINT: *Ask for Advice - Have you ever looked at a neighbor and wondered why they purchased a piece of equipment or made a particularly poor decision. Why didn't someone advise them? It can be beneficial to have a third-party view of your operation to assess your strengths and weaknesses. Sometimes farmers do not recognize the most obvious strengths or weaknesses due to denial, modesty, or some other reason. Finding someone you can trust to give you an honest evaluation can be critical to an accurate assessment.*

Opportunities and Threats - Evaluation of the External Environment

This part of the S.W.O.T. analysis focuses on existing external opportunities and threats. This section of the S.W.O.T. analysis allows the organization to identify strategies that take advantage of opportunities for growth while avoiding potential threats.

Opportunities and threats are external to the organization. The business owner cannot alter these events but instead must change with and react to the changing external factors.

Examples of opportunities and threats include *new or expanding markets, government regulations or incentives, new technologies, increasing competition, lower or higher barriers to entry, or changing economic conditions.*

HINT: An important step in starting your business and reaching your goals is to thoroughly research your state, county and town regulations on building construction, signage, animal numbers, processing and other laws that may affect the production or sales of your goods and services. You should call your County Extension Office, Zoning Office and Health Department for assistance and information.

A major focus of the external analysis is an evaluation of the competition. Chronicle all businesses competing in a similar area (product and geographic areas) as yours. List - their main customers, market share, product offerings, pricing objectives, and perceived marketing strategy.

Competitor #1
Name and Location of Company:
Product and Price Offerings:
Promotional Activities:
Competitive Advantages:
% Market Share:

Competitor #2
Name and Location of Company:
Product and Price Offerings:
Promotional Activities:
Competitive Advantages:
% Market Share:

Competitor #3
Name and Location of Company:
Product and Price Offerings:
Promotional Activities:
Competitive Advantages:
% Market Share:

Competitor #4
Name and Location of Company:
Product and Price Offerings:
Promotional Activities:
Competitive Advantages:
% Market Share:

List the external opportunities of the farm business.

List the external threats of the farm business.

S.W.O.T. Analysis

Use this chart to summarize your S.W.O.T. Analysis.

Internal Strengths:	**Internal Weaknesses:**
1. ____	1. ____
2. ____	2. ____
3. ____	3. ____
4. ____	4. ____
5. ____	5. ____
6. ____	6. ____
7. ____	7. ____
8. ____	8. ____
9. ____	9. ____
10. ____	10. ____
External Opportunities:	**External Threats:**
1. ____	1. ____
2. ____	2. ____
3. ____	3. ____
4. ____	4. ____
5. ____	5. ____
6. ____	6. ____
7. ____	7. ____
8. ____	8. ____
9. ____	9. ____
10. ____	10. ____

Step 3: Creating plans of action and identifying areas of competitive advantage

At this point, you have collected information and identified internal strengths and external opportunities. Now is the time to bring these two together and develop alternate plans that will capitalize on your farm business's strengths and opportunities, and mitigate weaknesses and threats.

As you think through the strategic planning process, do not try to immediately come up with the ultimate best strategy for your operation. You will need to consider all of your possible strategies based on the findings from the information discovery and S.W.O.T. analysis. Compare and contrast the competitive advantages of each strategy and select the best. This should be an ongoing, creative process. If you find this phase difficult, break apart the process and start with information discovery and then focus on the marketing strategy phase.

HINT: Plans of action include specific areas that utilize your strengths and competitive advantages, such as efficiency, market access, and market penetration.

Things to think about when developing a plan of action:

Businesses will create competitive strategies to set themselves apart from others in the market. Least cost and differentiation are two competitive strategies.

A least-cost strategy focuses primarily on product price or cost. Having the least expensive product in the market assures a competitive advantage. This strategy involves cutting input costs and often providing a "no frills" product. A least-cost strategy normally focuses on efficiency of operations. Most commodity-based industries such as grain, utilize a best or least-cost strategy.

Generally small farms lack economies of scale and cannot compete in a commodity market based solely on price. Instead, you will want to focus on some unique or differing attribute that offers the customer perceived value.

A differentiation strategy distinguishes the differences of a product to make it more desirable to a specific market. The strategy focuses on goods and services to satisfy the customer where the value outweighs the increased cost. A differentiation strategy also sets your product apart from the competition, creating a competitive advantage by offering a unique or different product or service from other companies.

For small farm enterprises, especially those with specialty crops,
the differentiation strategy is most popular.

The questions below will provide some tips for outlining a differentiation strategy including your product, attributes and pricing:

1) What is unique or different about your farm business (products and/or services)? Unique attributes may include: production methods, packaging, location, availability etc. What is the competitive advantage garnered from your strategy?

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2) The product/service attributes should be unique enough that other competitors cannot easily copy it, but adequate enough to capture a sustainable market share.

List why your product or service will not be easily copied and why your customers will buy from you:

HINT: Think about consumer benefits, market research and competition. What do your consumers want in the product and what are they willing to pay?

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List the various strategies that you could implement on your farm.

Step 4: Selecting the best plan that fits your overall farm mission

It is now time to review steps 1-3 and select the plan that best fits your overall farm business. Keep in mind your business's strengths and weaknesses as well as external opportunities and threats. Once all of the possibilities have been laid out and the best strategy chosen, be sure it fits with your farm mission and objectives. Can you see yourself doing this in 5-10 years?

The overall strategy is derived from components including marketing, production, operational, financial, and management strategies. Be sure to include the main components of marketing, production, finances, management, and your key competitive advantage points.

HINT: *At this point in your plan, you may want to wait and complete this task after analyzing the marketing and financial sections.*

My Overall Farm Strategy:
This is a short and concise summary of your strategy stated in three or four sentences.

____

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Step 5: Implementing and evaluating the strategy

An Implementation Plan is very important. This is how you will "get it done." The section following the Management Plan focuses on how to implement your strategy.

Be sure to **review and evaluate** your plan periodically. Demographics, markets, competitors and SWOT may change over time. As you update your plan, you will also want to revise your farm strategy.

MARKETING STRATEGY AND PLAN

Marketing your products and services is essential to farm profitability and viability, yet many farms lack a specific, organized plan. A producer should have a detailed plan describing how he/she will market products, services, and/or attractions.

Now that you have formulated an overall farm strategy, much of your marketing homework is complete. You understand what customer's value and why they would buy your product. The marketing plan will detail how you will create and convey value to the customer. Consumers derive value from the four P's of marketing--product, price, placement, and promotion.

It is important to recognize that the marketing plan is much more than advertising your product; it is the entire plan of how you will convey value, both real and perceived, to the customer. The promotion part of your marketing plan should include advertising. Promotion can also include your website, social media and other web-based features.

When developing a marketing strategy, think about ALL possible alternatives. Be creative.

Target Market - it is important to understand who is purchasing your products so that your marketing efforts will reach that segment. You cannot be everything to everyone. In order to effectively market, you need to cater your product and services to the set of customers who will see value in your product. *Who are you marketing to?*

Your target market identifies who is mostly likely to purchase your product, allowing you to appropriately market to them. Understanding your target consumer will make your marketing efforts more effective.

You can develop your target market by considering:

- Demographics—age, gender, family size, education, occupation
- Geographic—location, city, urban, rural
- Psychographic—behavioral patterns, lifestyle similarities, common interests, beliefs, and hobbies

Refer to University of Maryland Extension Factsheet FS-846 for more information on marketing and the UME Ag Marketing website at www.extension.umd.edu/agmarketing.

Marketing Situation

We covered market research in the "Developing a Strategy" section. Use that information in your marketing plan to develop a specific target market.

Who is (are) your target market(s)?

How can you reach this (these) target market(s)?

Marketing Objectives

Your marketing objectives are an important part of the marketing plan. This is where you record your short and long-term marketing goals. Objectives can include new product lines, market expansion, sales goals, customer base and promotional efforts. These may change with time and market trends. As with your business goals, be sure to keep them SMART.

Short Term:

Long Term

Components of a Marketing Plan

This section of the marketing plan addresses the four P's of marketing.

Product - *What sets your product apart from others? What are the product's main attributes? What are you really selling?* This includes anything that has to do with the product or service, including production, packaging and quality. It is a detailed list of the features and benefits of your product. Sizing, slogan and logos are other considerations for your product.

Price - *How much value does your product offer? How are you going to make pricing decisions?* The product's price is an important factor in your marketing plan. Find a price that will satisfy both you and your buyer. The starting point is to determine your cost of production and break-even price using an enterprise budget that includes returns to labor and management. This establishes the lowest price you can charge and still cover your costs. You will then choose one of three pricing strategies that take into account your cost structure and you competitors' strategies.

- Low price: This strategy is used by low-cost, high-volume producers who can compete directly with other producers on price. Most small businesses do not have the economies of scale or the volume of production to use this strategy.
- High price: This strategy is used by producers who have higher-quality products and services compared to other producers. Customers want your product because it is the best and are willing to pay a higher price. Producers with a niche market use this strategy. You are the only one producing a product that customers want and so you can charge a higher price. Examples include ethic/heirloom vegetables, early/late season vegetables or organic vegetables. This strategy is also used when you have added value or your products are somewhat different from your competitors. Examples are products that are processed or packaged to provide extra value. The price differential between your product and the standard product should not outweigh the value of the difference. This is a common pitfall for small farmers and should be carefully tested with focus groups and sampling offerings as part of the marketing plan.
- At-the-Market: This is a common strategy where the price is the same as your competition. Your product quality is not noticeably greater than your competition so customers will not pay a higher price. Profit could be improved through "Place" and/or "Promotion" strategies.

Place - *Where will you sell your product? Where does your target market shop?* This focuses on where your product is being sold and how it is distributed. Small farmers selling directly to the customer capitalize on this marketing point. Also, remember that consumer's value convenience, which means time, can be an important component of the distribution theme. You should address logistical issues such as transportation, warehousing, direct selling, wholesaling, storage and inventory management. The local food movement and Internet sales have significantly changed the distribution avenues. Selling via the Internet and delivering to the customer's door in another state, region or country is easier than ever before.

Promotion - *Where is the best value for your promotional money and efforts and how will you determine if they are working?* Promotion, including advertising, market position, sales and media connect your product to the consumer. Ideas for promotion include brochures, websites, social media, print ads and signage. Promotional materials should focus on attributes, features and benefits valued by consumers. Think creatively about how you communicate your product to the consumer. Design your product promotion for the target market.

In the marketing plan, think of each enterprise, product or service that you produce and consider the product itself, placement in the market, pricing and promotion.

Use the following charts to develop marketing ideas and ultimately, a plan to sell. Use a separate chart for EACH product/service that you offer:

- **Product:** Describe your product or service in detail, including product features and benefits.
- **Price:** Describe your pricing strategy and payment policies.
- **Place:** Describe how and where you will place your product so customers have access and you will make the sale.
- **Promotion:** Describe the promotional tools or tactics you will use to accomplish your marketing objectives.

Be sure to address marketing duties in the Management Plan. Who is responsible for jobs within Product, Price, Place and Promotion?

Product	
Price	
Place	
Promotion	

Product	
Price	
Place	
Promotion	

Product	
Price	
Place	
Promotion	

Product	
Price	
Place	
Promotion	

Marketing Budget Plan

Category	Quantity	Cost	Total	Notes
Research				
Research hired				
Web research				
Research publications purchased				
Communications				
Promotional brochures				
Radio/television				
Web design/maintenance (social media)				
Networking				
Memberships/affiliations				
Events				
Subscriptions				
Promotions				
Product giveaways				
Product discounts				
Special offers				
Advertising				
Brochures (development/printing)				
Logos/labels				
Packaging				
Signage				
Mailings/postcards				
Radio/television				
Newspapers				
Public Relations				
Charity events				
Advertising				
Employee promotions				
Sponsorships				
Distribution				
Shipping				
Transportation				
Marketing Total				

***Marketing expenses and labor should be included in the enterprise budget.**

ENTERPRISE BUDGETING

Small farms will often consist of many different enterprises that contribute to the whole farm operation. For instance, one farm operation may have a retail produce market, horse hay sales and a fall petting zoo. It is important to understand the returns, various costs and ultimately the profitability of each enterprise. The "enterprise budget" enables you to do that.

Income

It is important to generate good estimates for sales quantity. Your sales are determined by yield and price. As you estimate your gross income, remember that income should be based on products sold, not total production yield. Harvest loss, damaged goods, transportation loss, storage loss and unsold production can affect production. The general term used for this loss is "shrinkage". Be sure to include shrinkage when entering the quantity of goods sold in the enterprise budget.

Costs

The enterprise budget separates and allocates the various farm expenses and receipts to a particular enterprise. As a result, you can understand break-even cost and pricing points for each enterprise. It is also helpful to understand the input structure, such as shelf space pricing structure, raw material inputs, fixed equipment cost and labor inputs. Operator and family labor costs are an important and often overlooked expense. Be sure to include an expense line in your enterprise budget to address these costs, which can include expenses for office work, marketing, repairs and networking.

Budgets

The enterprise budget also forces you to analyze the profitability of each enterprise so you can achieve the proper enterprise mix for the farm. In order for enterprise budgets to be effective, you must have accurate information on each planned enterprise. This requires careful recordkeeping of existing enterprises and detailed projection of the activities of planned enterprises.

The budget is calculated based on a one-year period for a certain unit of production, such as an acre or per head of livestock. Figure 1. illustrates the enterprise budget components.

Example enterprise budgets are available at the Maryland Rural Enterprise Development Center, www.extension.umd.edu/MREDC

Figure 1. Components of an Enterprise Budget

Total Income: The total sales of product or services from the enterprise. Calculate revenue with the following formula:
Price x Units Sold= Total Income

⇩

Variable Cost: The cost of items that vary with production volume. Examples include fertilizer, seed, fuel, electricity, labor charges, pesticides, packaging cost and custom charges.

⇩

Fixed Cost: Those costs that you incur regardless of whether you produce any output. These costs are determined using the DIRTI 5 method --Depreciation, Interest, Repairs, Taxes, and Insurance. Often a producer will use a piece of equipment or building for more than one enterprise. In these cases, it is important to estimate the percentage of use for each enterprise and allocate the cost accordingly.

⇩

Net Income: Net income is the money left after subtracting variable and fixed costs. This is the bottom line.
NET INCOME = Total Income – (Variable + Fixed Costs)

ENTERPRISE BUDGET FORM **Enterprise>** **Unit>**

ITEM	UNIT	QUANTITY	PRICE	TOTAL
Income				
Total income				
Variable/operating expenses				
Total variable expenses				
Fixed/overhead expenses				
Total fixed expenses				
Total variable and fixed expenses				
Net income over variable and fixed expenses				
Break-even price (total expenses/yield)				
Break-even yield (total expenses/price)				

Methods of Analyzing the Enterprise Budget

The enterprise budget can provide a producer with much more information than net income. The budget can help determine sales needed to cover variable costs, fixed costs and total costs per unit. This information can be utilized to determine pricing points, to identify efficiencies within the enterprise, and for the continuation of an enterprise. The chart below describes various analysis methods.

Break-even Analysis		
Enterprise Analysis Methods	**Formula**	**Comments**
Variable Costs per Unit Sold	Total Variable Cost/Output in Units	You must make at least the variable cost per unit sold, or the enterprise should be discontinued.
Fixed (Overhead Costs) Costs per Unit Sold	Fixed Cost/Output in Units	In order to be profitable over the long run, you must be able to cover the fixed and variable costs. Knowing the fixed cost per unit enables you to better understand cost structure.
Break-even Price	Fixed Cost + Variable Cost/Output in Units	You will need a pricing point above the break-even point to generate a profit.
Break-even Output	Fixed Cost + Variable Cost/Price per Unit	This is the output needed at a given price to reach the break-even point. At the given price, you will need to expand output to increase net income.
Net Income per Unit Sold	Net Income/Output in Units	This is the net income per unit produced.

FINANCIAL PLAN

A financial plan will be one of the most important pieces to your plan. This section will detail the assets, liabilities, profit, loss and cash flow for the business. The plan will use historical information for existing businesses and projections for starting businesses.

Three financial statements can describe the financial position and performance of a farm. These statements are generated by organizing and analyzing your business's accounting activities. While financial statements take some research and homework, they are necessary to your farm business.

Financial Statements help you:

- Determine your farm's solvency, profitability and liquidity
- Make important production, financing and investment decisions
- Help with credit and lending applications
- Develop budgets for farm enterprises

Projections

It is important to project 3-5 years of financial statements for your farm business depending on a loan application, long-term goals or a new enterprise decision. Projected financial statements also are referred to as *pro forma* budgets. By projecting your business's financial statements, you will discover whether you can anticipate long-term profit.

Projections are based on the income and cash flow statements. Projections are a business owner's best estimate of income and expenses over a period of time. Being conservative and realistic with your projections will help your business in the long run.

The best way to start making any projections is to review your enterprise budgets and financial statements. From there, you will be able to predict average costs and expenses over time. The pro forma financial statement should reflect your implementation strategy and sales projections.

Creating a financial plan can be a complex process. You may need additional spreadsheets to assemble information and budget totals. For help and examples, visit www.extension.umd.edu/MREDC.

Along with projections, you also may want to conduct financial ratio analysis for your farm. This will look at long-term projections and costs and answer questions regarding liquidity, profitability and debt.

The three financial statements show different financial measures for a business.
Balance Sheet (Solvency): A detailed listing of assets, liabilities and net worth at a given point in time. It answers the basic question, "How much is your farm business worth?"

Importance - Net worth is the best measure of a farm business's financial position. It organizes what the producer owns (assets) and owes (liabilities), which ultimately determine farm solvency. *What is your farm business's financial position?*

Income Statement (Profitability): A listing of income, expense, and profit for a farm operation in a calendar year. This statement includes inventories and depreciation.

Importance - Profitability is the summary of all resources that came into the farm (revenue) and left the farm (expenses). This equals the net income or net loss. *How did the farm business do last year?*

Cash Flow (Liquidity): Records time and size of cash inflows and outflows that occur over a calendar year. Liquidity differs from profitability because the cash flow statement only includes cash income or expenses. In contrast, the income statement includes non-cash items, such as depreciation and inventory adjustments.

Importance - Liquidity is the ability to generate enough cash from your farm enterprises to meet financial obligations without disrupting normal business operations. The cash flow statement is a critical component of the business plan and will be reviewed by lenders. *Where is cash used and can bills be paid on time?*

Table 1. summarizes the differences between the projected income statement and cash flow budget.

Table 1. Projected Income Statements Show Potential Profitability While Cash Flow Budget Summarizes Farm's Liquidity

Projected Income Statement	Cash Flow Budget
	Beginning cash balance
Cash income	+ Cash income
- Cash expenses	- Cash expenses
- Depreciation	+ Capital sales
= Profit (Loss)	- Capital purchases
	+ Loan receipts
	- Loan principal payments
	+ Nonfarm receipts
	- Withdraws
	= Ending cash balance

Balance Sheet

The balance sheet shows assets on the left and liabilities and net worth on the right.

Asset - the items owned by the farm business, such as land, buildings, machinery, livestock, crops in storage and supplies.	*Liabilities* - the debts owed by the farm business, such as notes payable, interest, taxes, loans and rent.

Farm assets and liabilities are divided into three categories according to their length of life, cash liquidity, and effect on farm business production. The categories are current, intermediate and long term. A fourth category lists non-farm assets.

There are two possible methods for estimating asset value: Market Value or Cost Approach.

Market Value:	Values assets at the estimated current market value.
Cost Approach:	Values assets at their original cost plus cost of improvements minus depreciation.

Current Assets/Liabilities - are those with a less than one year of life. Assets include cash, accounts receivable, and other assets easily converted to cash within a year. These can include prepaid expenses, supplies, crops and livestock on hand. Liabilities consist of accounts payable and accrued expenses such as rent, interest and taxes that will be paid within one year. Short-term notes and the current principal due on longer-term liabilities are also listed.

Intermediate Assets/Liabilities - are those with a life of more than one year but less than 10 years. Assets include breeding livestock, tools, vehicles, machinery and equipment. Liabilities consist of loans for breeding livestock, machinery and equipment.

Long-term Assets/Liabilities - are those with a useful life of more than 10 years. Assets include farmland, buildings and improvements. Liabilities consist of mortgages and contracts owed on farmland and loans for buildings and improvements.

Non-farm Assets/Liabilities - these are personal items not considered part of the farm operation. Assets include the home, furnishings and vehicles.

Net Worth is sometimes referred to as owner's equity. It is the difference between the value of farm assets and the liabilities against those assets.

ASSETS – LIABILITIES
= NET WORTH

BALANCE SHEET Date

ASSETS			**LIABILITIES AND NET WORTH**	
Current farm assets		**Value**	**Current farm liabilities**	**Value**
Cash, checking, savings			Accounts payable and accrued expenses	
Prepaid expenses and supplies				
Accounts receivable				
Inventory held for sale/feed	Quantity			
			Intermediate/long-term principal due <12 months	
Other current farm assets				
Total current farm assets			Total current farm liabilities	
Intermediate farm assets			**Intermediate farm liabilities**	
Total intermediate assets			Total intermediate farm liabilities	
Long-term farm assets			**Long-term farm liabilities**	
Total long-term farm assets			Total long-term farm liabilities	
Non-farm assets			**Non-farm liabilities**	
Total non-farm assets			Total non-farm liabilities	
Total Assets			**Total Liabilities**	
			Net Worth (Assets – Liabilities)	

Projected Income Statement

Producers should develop a projected income statement, sometimes called the projected profit and loss statement, to forecast farm profitability. A projected income statement estimates future income, expenses and profit for the business. The statement will cover a given accounting period such as a calendar year or other fiscal period.

Projecting an income statement is easier if there are historical income statements to use as a reference point. Enterprise budgets also are an important aid. Enterprise budgets estimate income and expenses on a per-unit basis. You can develop your projected income statement by multiplying the income and expenses in the various enterprise budgets by their respective total number of units and adding them together.

During start up and transition periods, some businesses will need to develop projected income statements over several years. Long-term projections are especially important for businesses that will have escalating sales volume over multiple years, large inventory differences from year to year (such as perennial crops or nonperishable goods) and businesses with enterprises starting in different years.

Cash Farm Income - List sources and values of your cash farm income. Include revenues from sales of crops, livestock, livestock products, as well as payments from federal commodity programs. Also, include income received for custom work, co-op dividends and other sources.

Cash Operating Expenses - Include expenses associated with operating the farm business. In addition to variable production expenses such as feed, seed, fertilizer, and short-term interest on operation capital and supplies, include fixed cash expenses such as taxes, insurance and interest on intermediate and long-term loans.

$$\text{Depreciation} = \frac{\text{beginning value} - \text{ending value}}{\text{years of useful life}}$$

Depreciation - Even though depreciation is not a cash cost to the operation, it should be included in the income statement because it represents the loss in value of buildings, machinery and other assets that wear out as a result of production. Without depreciation, the income statement will not account for these economic losses. Historical depreciation can be a starting point for estimating future depreciation, but you must also consider the depreciation of future machinery and building purchases included in the business plan. A simple way to estimate annual depreciation is to take the purchase price (beginning value) of the equipment and buildings, subtract the salvage (ending) value and divide by the number of years of useful life

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Profit or Loss - The projected income statement should give a picture of future business profit. As the business changes, there is often a transition period where profits may vary year to year. If this is the case, you may want to develop a projected income statement for each year until the business reaches a steady state. As your plans progress, you will want to have a good accounting system in order to construct historical income statements to analyze the progress of your business.

PROJECTED INCOME STATEMENT **Period covered>**

CASH FARM INCOME		CASH FARM EXPENSES	
Source of income	**Value**	**Description of expense**	**Value**
Crop sales		Production expenses	
Livestock sales			
Government payments			
Other income		Other expenses	
Total cash farm income		Total cash operating expense	

Depreciation schedule				
Asset	Beg. value	End value	Years	Depreciation
Total depreciation				

Net cash farm income (income - expense)	
Profit or Loss (net cash - depreciation)	

Cash Flow Budget

The cash flow budget is another important financial statement. It is used to estimate the flow of money in and out of the business. It is similar to the projected income statement in that contains estimates of the cash income and cash expenses. However, there are important differences. The cash flow budget does not include depreciation since it is not a cash expense. Rather, it will include the actual purchase prices for capital – (machinery and buildings) purchases. The cash flow budget will include sales of capital assets, cash flowing into the business from loans, including loans for machinery and buildings and loan principal payments. It includes other receipts from non-farm sources as well as withdraws.

The cash flow budget estimates the timing and size of cash inflows and outflows that occur in a given accounting period, normally one year. The period is broken down into smaller time periods such as quarters or months. Think of the cash flow budget as a checkbook for the farm with an accounting of deposits and withdrawals. Here is an explanation of cash inflows and outflows.

Cash inflows	Cash outflows
• *Crops and livestock sales* - the primary source of cash for your farm business and are critical to maintain the liquidity reserve. • *Other farm receipts* - includes payments from government programs, custom work, and co-op dividends. • *Non-farm receipts* - includes items such as income from an off-farm job, savings, investments, interest earned and capital. • *Capital sales* - includes the sporadic cash inflows from the sale of land, buildings, machinery, breeding livestock and tools. • *Borrowed money* - is considered a residual source of cash used to maintain your liquidity reserve when cash outflows exceed the sometimes sporadic inflow.	• *Production expenses* - are a large draw on your liquidity reserve. They include seed, feed, fertilizer, chemicals, hired labor and repairs. • *Capital expenditures* - include cash outlays for replacing and adding machinery, breeding livestock, land and buildings. These are important to your farm but should be planned carefully. • *Loan payments* - are payments on borrowed money. Consider this when formulating your loan payment schedules and the seasonality of your farm business. • *Family living expenditures or withdrawal* - are sometimes overlooked as being secondary to the other cash outflows.

The cash flow budget is projected at the beginning of the year to forecast the inflows and outflows and estimate the ending cash balance for each quarter or month. As the year progresses, keep an **actual cash flow statement** to record cash transactions as they take place. Then compare the actual and projected cash flow statements to see if things are going as planned, to devise remedies for unforeseen problems or to take advantage of opportunities not anticipated. At the end of the year, use the actual cash flow statement to estimate the projected cash flow for the next year. This is especially important for agricultural businesses because of production cycles and the seasonality of the business.

CASH FLOW	Last year	Year 1 or 1st quarter	Year 2 or 2nd quarter	Year 3 or 3rd quarter	Year 4 or 4th quarter	Total
CASH INFLOW						
1. Beginning cash balance						
2. Crop sales						
3. Livestock sales						
4. Other farm income						
5. Capital sales						
6. Non-farm receipts						
7. Total cash inflow (total 1 to 6)						
CASH OUTFLOW						
8. Chemicals						
9. Custom hire						
10. Feed purchased						
11. Fertilizer and lime						
12. Freight and trucking						
13. Gasoline, fuel, and oil						
14. Insurance						
15. Labor hired						
16. Rent or lease						
17. Repairs and maintenance						
18. Seeds and plants purchased						
19. Supplies purchased						
20. Marketing						
21. Taxes						
22. Utilities						
23. Vet., breeding, medicine						
24. Other farm expenses						
25. Capital purchases						
26. Family living or withdrawals						
27. Term loan payments						
28. Total cash outflow (total 8 to 27)						
CASH FLOW SUMMARY						
29. Inflow minus outflow (lines 7-28)						
30. New borrowing: term						
31. New borrowing: credit						
32. Credit line payments						
33. Ending cash balance (29+30+31-32)						

MANAGEMENT PLAN

Farms need people just as they need land, equipment, and materials. A management plan should identify the jobs needed on the farm and who will be responsible. Having this clearly communicated within any business is important. A management plan should try to capture the "people element" of what a farm is hoping to achieve.

A management plan also identifies legal and liability issues of hiring and managing employees. Depending on the type of farm business and employee structure, it is important to research Maryland's employee laws before hiring and which may apply to your business.

Parts of the Management Plan

- *Position and Duties* – organizes the job title, position or name of the job that must be completed. Examples include manager, marketer, mechanic, farm worker, sales and so on. Include the duties and responsibilities for that position. List the skills and talents required for the position, as well as the salary and wages. Finally, indicate if the required work schedule is full time, part time, seasonal or contractual.
- *Organizational Chart* - arranges the structure of a business by rank. This chart is helpful to know who is responsible for the different parts of the business.
- *Skills and Training* – will list the skills, training, and continuing education needed for the business to be successful. This list will catalog new technologies or skills that can be adapted to the farm business, as well as the responsible party.

A management plan addresses:

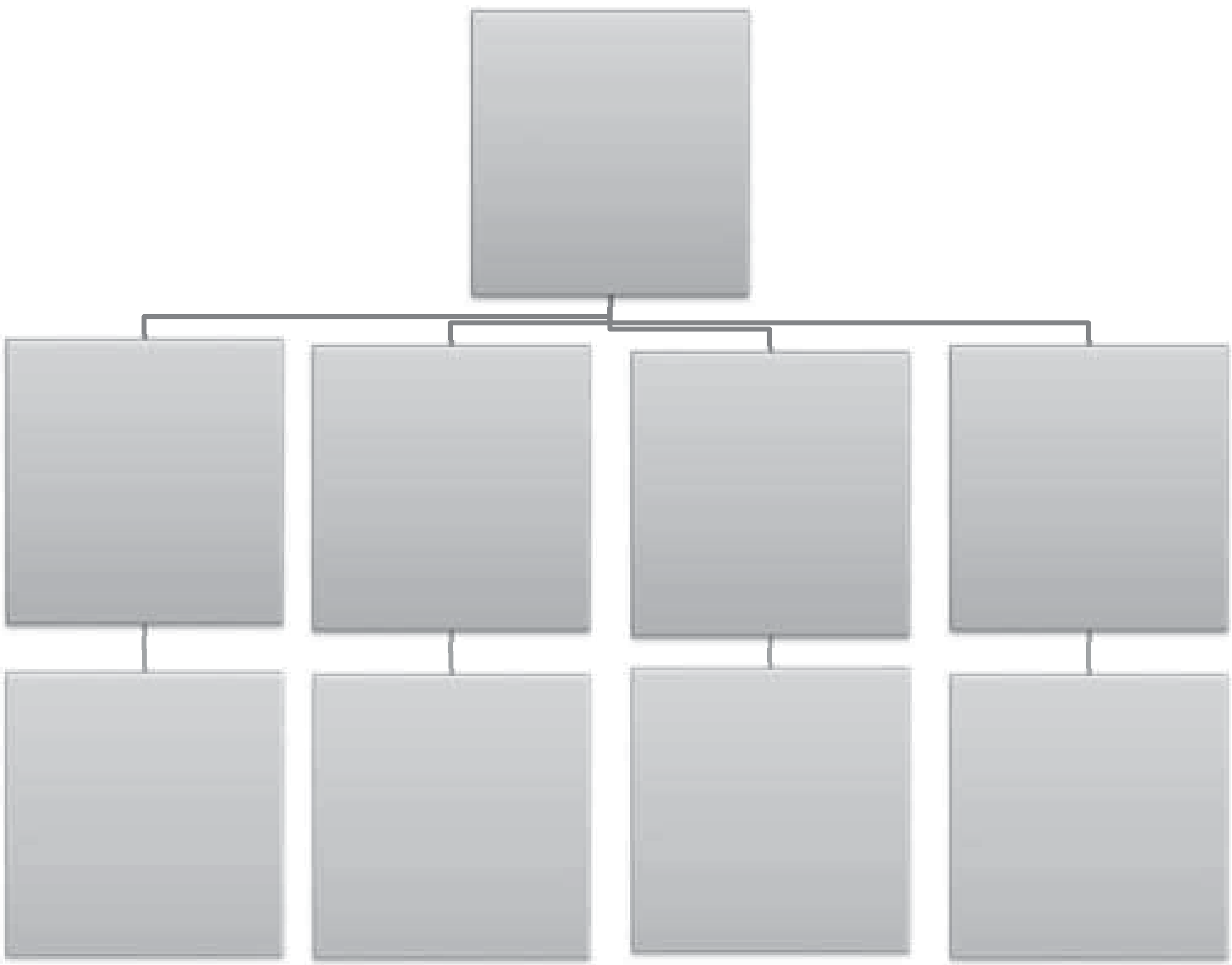
- Are the right people in place?
- Does the farm business have the appropriate mix of skills?
- Does the farm business have access to advisors, consultants and professionals for assistance?
- Is there a hiring process, which communicates the businesses vision, policies and expectations?
- Do employees display the proper attitudes and behaviors?
- Are employees developing suitably?

Use this chart to layout positions within your farm business, the duties of each position and who is responsible.

Farm Business Positions and Duties				
Position/Name	**Duties/ Responsibilities**	**Skills/Talents**	**Salary/Wages**	**Work Schedule**
1.				
2.				
3.				
4.				
5.				
6.				
7.				

Farm Business Organizational Chart

An organizational chart arranges the structure of a business by rank. This chart is helpful to know who is responsible for parts of the business.



Skills, training and continuing education are the last components of the management plan. What skills are needed or necessary for the farm business? Are there any new technologies or skills that can be adapted to the farm business?

Skills and Training		
Skill	Training Available	Responsible Party

IMPLEMENTATION STRATEGY

You have done your homework, conducted market research, and developed areas of competitive advantage. All that is left is collecting the paycheck, right? Not so fast. The formation of an optimal strategic business plan is useless unless the plan is implemented. In other words, a correctly devised business plan is often said to be "The right thing to do," while the implementation of the plan is considered "Doing things right". An organization must be able to accomplish both if it is to remain successful.

The implementation plan will contain a timeline for the steps needed to meet business objectives. Consider the implementation plan your ultimate "To-Do List". The timeline will cover the production, financial, management and marketing goals outlined in the business plan. As you develop the implementation plan, you may begin to notice areas where the best-made plans are not practical. Taking time to go through this process will help you identify bottlenecks and avoid pitfalls.

The implementation plan contains the following information:

Time:
- This is the timeline for tasks. It can be days, months or years.

Production:
- Products or services produced and projected production
- Timeline of production changes, new enterprise development

Marketing:
- Sales projections
- Expected price
- Marketing locations and customer base
- Market entry—promotion

Finance/Accounting:
- Identify funding mechanisms
- Timeline of when capital will be needed or purchased
- Method of accounting and recordkeeping
- Method of paying taxes and meeting requirements

Management:
- Division of duties and responsibilities for tasks
- Labor sources needed
- Labor management plan—training, skills development
- Plan for payroll, taxes, and benefits

Implementation Plan

Time Period	Production	Financial	Management	Marketing

EXIT STRATEGY

Operating a farm business includes many risks. Though you may never intend to quit, sometimes it may be the best decision for your family. Common reasons for exiting the business can include poor profitability, illness, death of a partner, generational transition, financial issues and age.

It is prudent to consider an exit strategy from the market. This plan should include a set of criteria that signal you that it may be time to exit the business.

Such signals can include:
- Farm profit/loss
- Pre-determined age
- Estate plans and farm transfer
- Change of markets

Exit Strategy

RESOURCE INVENTORY

Gathering and analyzing resources is an efficient and prudent exercise for any farm business. Many small businesses and small farms purchase brand new and sometimes unnecessary equipment, buildings and machinery. These expensive capital purchases can overextend a business if you have not done planning and analysis.

The first step in creating a resource inventory is to step back and look at your whole operation. Evaluate what resources are available to you and include all those needed to carry out goals of the operation. As the inventory is completed, multiple or complementary uses may stand out.

This section includes:

- Building and facility requirements – these are physical resources owned or available to the business. It includes land, livestock, equipment, facilities, transportation, expertise and other physical needs. Include those owned, leased or needed.
- Building and structure inventory – includes more in-depth information about the facilities for the business. Your inventory should include the building, purpose, square footage, required features and the location.
- Equipment inventory – includes the name of the equipment, model and serial number, model year, year purchased, equipment condition, ownership, purchase price and market value.

A resource inventory can help:

- Complete a balance sheet
- Summarize collateral for a loan
- List the conditions of assets and identify problems
- Evaluate options and needs for growth and/or diversification
- Document resources in case of fire, theft or damage

Building and Facility Requirements	
Physical Resources	**Description of Resource and Use**
Land:	
Livestock:	
Facilities: (more detailed worksheet follows)	
Equipment: (more detailed worksheet follows)	
Transportation:	
Expertise: Computers, marketing, record keeping, etc.	
Other:	

Building and Structure Inventory

Building	Purpose	Square Feet	Required Features	Location
1.				
2.				
3.				
4.				
5.				
6.				

Equipment Inventory

Name	Model and Serial	Model Year	Year Purchased	Condition			Ownership			Purchase Price	Market Value
				G	F	P	O	L	B		

Condition—G=Good, F=Fair, P=Poor
Ownership—O=Owned, L=Leased, B=Bought

APPENDIX

Documents that can be included in your Business Plan Appendix:

- Corporation or partnership documents
- Personal resumes of owners and key personnel
- Credit report
- Farm maps
- Copies of leases, significant agreements, and contracts
- Enterprise budgets
- Other documents relevant to the business plan

Contact List

Name	Address	Phone	Email	Website

Business Web Resources

University of Maryland Extension
www.extension.umd.edu
- Beginning Farmer Success www.extension.umd.edu/newfarmer
- Ag Marketing www.extension.umd.edu/agmarketing
- Maryland Rural Enterprise Development Center www.extension.umd.edu/mredc

eXtension—Entrepreneurship
www.extension.org/entrepreneurship

FormNet—Free Business Forms
www.entrepreneur.com/formnet

Maryland Department of Agriculture
www.mda.maryland.gov

National Sustainable Agriculture Information Service
www.attra.ncat.org

Ag Plan
www.agplan.umn.edu/

U. S. Small Business Administration
www.sba.gov

U.S. Department of Agriculture, Farm Service Agency
www.usda.gov
www.fsa.usda.gov

U. S. Census Reports
www.census.gov

Value-added planning and business development
www.agmrc.org/business_development