Security Bank

FINANCIAL**FOCUS**

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HOW CAN YOU KEEP YOUR LINE OF CREDIT OPERATING SMOOTHLY ?

Here it is! We are about to the end of 2019. We all know that this year has had its share of challenges in farming and other things, but hopefully as our November article pointed out, you can look back and find many positives as well. For us, it now becomes the equivalent of our "harvest" time as we dive into the busy process of farm line of credit renewals. As you know, your renewal process starts with a year-end balance sheet. This month let's review the very basics of what usefulness a balance sheet provides.

From all of us at Security Bank, have a Happy Holiday Season!

Best Regards!

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PRESIDENT/CEO
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BALANCE SHEET 101:
"BACK TO THE BASICS"

BY ***LEE POTTS*** | *Vice President/Loan Officer*
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Harvest should be wrapped up, so now starts the process of assessing how the year went overall and planning for 2020. This past year certainly has presented some challenges, and we know that 2020 will have its own set of unique scenarios. You will soon be sitting down with your lender to put year-end numbers together and see where things stand after this interesting (but hopefully rewarding) year. As lenders and producers gear up for those conversations, we thought it would be beneficial to go back to the very basics of the balance sheet, or a "balance sheet 101," if you will, to review exactly what the balance sheet represents.

In my own personal words, a balance sheet is a snap-shot of one day in time of one's financial condition. No different than a snap-shot of the family at Christmas time. In the following days from that date, the people in the photograph continue to change in various ways. The same is true with a balance sheet. You could do a balance sheet the next day, and it would look different—maybe only slightly different, granted, but different nonetheless.

Follow these handy tips to make sure the process of doing your balance sheet with your lender is a smooth process. Smooth and accurate entry of the numbers can more quickly lead to what matters more: *interpretation and deeper discussion!*

Have all inventories, accounts receivable, accounts payable, prepaids, head counts, bushels, and contracted amounts and prices (if any) ready.

Take some time to evaluate how your equipment values may have changed. We utilize websites like Machinery Pete and Tractorhouse.com to get a ballpark of what various things might be worth currently. Also keep track of equipment traded, sold, purchased, etc.

If there is financing outside of the bank, have the details of those loans ready as well. Loan balance, interest rate, payment amount, payment date, and maturity date.

If you utilize hedging, it makes sense to enter the "net liquidating value" of your hedge account (representing what your broker would send you if you liquidated positions that day) and then listing the grain inventory at current cash price (since that is what you would get if you liquidated grain that day also). This will reflect an accurate overall grain value while considering any equity you have in hedges.

Amounts owed to suppliers such as deferred seed or other inputs (can be included in accounts payable).

You gave all that info to your lender, so, what does a balance sheet tell you, the producer, and what do we focus on as lenders? Here are the Top 3 analysis points that are important in your balance sheet.

1. Net Worth/Equity/Earned Equity: Probably the most obvious measure is that of one's net worth or equity, which is simply equal to assets minus liabilities. Remember that asset values should be realistic each year as to what the grain, livestock, machinery, land, etc, might be worth in terms of a fair market value. Earned equity is measured by looking at the change in equity from the year before, and then adjusting that change for any manual changes to asset values such as machinery, breeding livestock, or land, for example. Think of the Earned Equity change as your defensive line (if comparing to football), which is your first line of defense against challenges from weather, markets, repairs, and many other things running straight at you. Strong earnings lead to the next two points discussed below being stronger. Side Note: We won't go into the philosophy of borrowing against land values for today's purpose, but you might refer to articles we sent earlier in 2019 for how that is often looked at.

2. Working Capital: You may recall that there have been several articles over the past couple years dedicated to this topic, as we consider it a big one. Subtracting Current Liabilities from Current Assets on your balance sheet will equal working capital. This is operating capital from within the business. Perhaps you might recall from past articles that working capital is your second line of defense after strong earnings. Or think of it as your linebackers, using the football analogy. If your defensive line (earnings) isn't strong enough to defend against markets, weather, and other adversity, the impact will show up next in your working capital.

3. Debt Structure: With an accurate balance sheet, an evaluation of your debt structure can take place. If there appears to be red flags in your debt structure, they can be addressed head-on. Red flags might look like a certain type of asset financed on too aggressive a term; an equipment or real estate payment per acre that is too high (as we have talked about in past articles as well); to name just a couple. If earnings and working capital become depleted, your equity starts to erode. Or in football context, this is your safety and cornerbacks; i.e. your last line of defense that you would prefer to preserve at all costs. After all, you have worked hard for many years to build up the equity you currently have.

With these points in mind, make sure you take the time to look at your financial snap-shot with your lender. Like a photograph, this picture or snap-shot is also worth a thousand words!