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Statement of Cash Flows

Agricultural Business Management

Gary A. Hachfeld, David B. Bau, & C. Robert Holcomb, Extension Educators

A complete set of financial statements for agriculture include: a Balance Sheet; an Income Statement; a Statement of Owner Equity and a Statement of Cash Flows. The FINPACK software, developed by the University of Minnesota, generates each of these statements. Other software and paper products generate similar information. Key ratios and measurements covering Liquidity, Solvency, Profitability, Repayment Capacity and Efficiency have become standards in the agricultural industry, and are generated from these financial statements.

The "Statement of Cash Flows" examines how cash has entered and left our financial life during the year. We need cash to flow into our lives so it is available to cover our family living, pay our taxes, service the debt we are committed to, and to make investments in our business and personal lives.

Cash Flow and Net Profit are not the same thing. One could have sufficient profits but insufficient cash flow. Or, one's cash flow could be adequate but profits are lacking. A complete set of financial statements and proper analysis of them will show financial strengths and weaknesses.

The following paragraphs describe how the "Statement of Cash Flows" generated by the FINPACK software is structured. Other software or paper forms will organize the information in a similar way.

To complete a "Statement of Cash Flows", one must have a good "Balance Sheet" from the beginning of the year, another for the end of the year, and an accrual adjusted "Income Statement" for the year.

The "Statement of Cash Flows" begins by showing the farmer's "Beginning Cash Balance" (farm and non-farm). This is the cash and account balances that are shown on his Balance Sheet from the beginning of the year.

The "Statement of Cash Flows" is divided into three groups, each examining a different source of and use for cash. These are "Cash from Operating Activities", "Cash from Investing Activities" and "Cash from Financing Activities". We will look at each one separately:

- The first group identifies "Cash from Operating Activities". This is cash that came into the farmer's life from farm income and from non-farm income. The cash also leaves his life as he pays farm expenses. Family living takes cash out as does income tax and social security tax. These sources and uses are added up to produce "Cash from Operations". If his earnings (farm and non-farm) bring in more cash than what went out for living and taxes, then "Cash from Operations" will be a positive number (desirable). If more cash left, than came in, then this will be a negative number (not desirable).

- The second group identifies "Cash from Investing Activities". Cash is generated by the sale of assets (farm and non-farm), and is used in the purchase of assets (farm and non-farm). These sources and uses are totaled to produce "Cash from Investing Activities". If this total is a positive number, it is contributing cash. If it is a negative number, it is using cash. It is quite common for this "Cash from Investing Activities" to be a negative figure for farmers because of the nature of the farming business. The farmer must invest in assets which are expensive and usually by the time they are sold, many are old or obsolete with little value.

- The third group identifies the "Cash from Financing Activities". Cash is generated by borrowing money and is used up in the repayment of principal (the interest portion is an operating expense, and has already been counted in the farm expenses of the first category). Also shown in this category are inflows from gifts and inheritances received, and outflows from gifts given. These sources and uses are totaled to produce "Cash from Financing Activities". This figure may be positive or negative, depending on whether he borrowed more funds than he repaid or repaid more than was borrowed, and whether he received more gifts and inheritances than were given away

The “Cash from Operating Activities”, Cash from Investing Activities” and “Cash from Financing Activities” are then totaled to produce the “Net Change in Cash Balance”.

The “Net Change in Cash Balance” is added to the “Beginning Cash Balance” to produce the “Ending Cash Balance”. This number will be the same as the cash and account balance shown on the farmer’s Balance Sheet at the end of the year.

The “Statement of Cash Flows” is an interesting statement and can identify a number of things happening in your financial life. Perhaps the cash generated from the “Operating” part of your life was sufficient to fund some “Investing” and also reduce some debt “Financing” (this would be good).

Perhaps the “Operating” portion contributed cash but the “Financing” cash had to increase to fund the “Investments” made during the year (this may be satisfactory, as long as things stay in appropriate balance). Another scene (not a good one) would be that the “Operating” portion of your life was not sufficient to cover the living and taxes so debt “Financing” was needed to fund the rest of it, plus any “Investments” made during the year.

Another scene (not a good one) might find that the assets “Investments” are being sold off to fund the shortages in the “Operating” portion of their life, and/or to reduce debt.

It is important for the farmer to have good financial statements and analysis, and to understand them. After all, it is his financial life.

Caution: This publication is offered as educational information. It does not offer legal advice. If you have questions on this information, contact an attorney.