

# WATER STREET SMARTS

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## The Importance of a Report Card

Ken Rahjes interview with Darren Frye, President and CEO of Water Street Solutions.

Q: We have been talking for several weeks about what a financial analysis can do for your farming operation. It gives you a check up, measures your risk bearing ability and it helps determine your long term break evens. It also serves as a baseline and allows you to do feasibility studies about future purchases. I understand it is a report card too Darren. Is that correct?

A: It actually is and as you get into doing these financial analyses you can begin to chart the progress you make each year. It lets you see how your decisions are impacting your bottom line. It provides multiple data points that allow you to establish a trend. In that trend people can see if they are moving in the right direction or moving away from their goals. Some of those goals might be growth or expansion because it seems like farmers want to get bigger. They might have other goals such as better financial health, transition, succession planning or other things they want to do. They want to create new wealth and there is opportunity to bring in that next generation. Whatever their goals are, whether it is financial independence, growth or it is bringing in the the next generation it allows them to see if they are heading toward their target and moving closer to that goal.

Q: We talked about data points, but what kind are we talking about?

A: We are going to look at a number of things but one of the primary things that we talk a lot about with our clients is working capital. A banker likes to look at three things when he looks at your financials. The first is cash, the second is cash and the third is cash. Your working capital is how much you are willing to invest to each project verses how much will I lend to you. The changes in working capital as a percent of gross revenue from year to year are very important. We are going to look at that as a ratio. We are also going to look at things like net worth, which is calculated by taking your assets and subtracting your liabilities. How much of your assets do you own in equity verses how much does the bank still own that you are paying off, so that is your net worth. We are also interested in machinery inventory and how labor and machinery is matching up on a per acre basis. We will track that as we make modifications and plan. Does that affect the bottom line; is that showing up as a trend? Then you have your ratios that a lot of people want to talk about such as return on assets and return on equity. Those are obviously things you want to track but probably not at the top of the list. I think working capital, net worth and how you are managing some of your assets within machinery of inventory and human resources are going to trump return on assets and return on equity ratios.

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Q: How can the financial report card further help us?

A: It is going to reinforce the efforts you are making to move in that direction. Consultants who work with you also need feedback. When you're taking a trip from Omaha, Nebraska to Los Angeles, California you chart the progress you are making by looking back at your starting point and understanding how far you have gone and how far is left to go. This not only allows the producer to be in control of his business but also allows consultants who work with him to understand if their suggestions, modifications and the things they are doing are actually making a difference. Some of these things are gradual improvements, like moving in the right direction. It is kind of like going to a health club. You don't lose twenty pounds overnight nor will you get into better shape overnight. Yet if you commit to working out three times a week and eating better over time it is going to make a big difference. That is much like these financial changes. By charting this in report card fashion you can see your progress and it can inspire that grower to continue down that path. It is encouraging the heart and is very important to understand if I am making gains on this or not. If I am not, then why not? Then make those changes so you can move toward that goal.

Q: Is there a certain peace of mind that goes along with this whole process?

A: Absolutely. The whole piece of mind that comes with observations such as: look at these outcomes; look at how these positions are changing my results. If you are in an operation with partners, relatives or investors you also need to convince them of the need or benefit of a particular practice, consultant or product. Isn't it easier to show this when you can measure it and you can understand that this is having an impact on my overall business? And doing what is right for that enterprise? These financial metrics in discovery and tracking; these things help you to set more goals, understand what has been achieved and what has to be accomplished. All of these are going to enter into having better business practices. Good business practices are things you can measure, monitor and be held accountable for. It gives you the confidence to do that, to face the challenges and obstacles that face your business every day because you are focused on a goal. You are not brought down by the mundane things. You focus on this outcome and the end results. The report card will help you do that because it gives you feedback, gradual feedback over time. It gives you direction and shows you how quickly you are making that journey and it is positive reinforcement for the producers.