

Agricultural Economics Curriculum

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Development Partners Include:



Lesson 2. Activity 1 – Monitoring the Flow of Cash

Introduction

Many businesses that are first starting out need money to buy materials before they earn any profit. Starting a business can be expensive depending on what type of materials and assets you need. Because of the need for startup money, banks will provide loans to help the business pay for materials.

In order to secure most loans, banks will ask for a business plan. The business plan will include many budget documents including the enterprise budget you learned about in Lesson 1. Another important budget that banks want is a cash flow budget. Although similar to the revenue portion of the enterprise budget, a cash flow budget examines if an enterprise is feasible for the business or individual. This type of budget takes a detailed look at all sources of cash and the uses of the cash related to the enterprise.

Materials

Students will need to have the following materials to complete this exercise:

- Pencil
- Computer with access to Excel[®] or other spreadsheet program - or -
- Calculator

Student Instructions

In this activity, you will create a cash flow budget for a corn enterprise. In order to identify the correct values to use when creating a cash flow budget you will need to follow these rules:

1. Identify all **CASH** revenues and all **CASH** expenses. Non-cash revenue or non-cash expenses are **NOT** included in a cash flow budget. Examples of each follows:
 - Cash sources: beginning cash balance, crop sales, livestock sales, and capital asset sales
 - Uses of cash: cash expenses, purchases of land and purchases of depreciable assets (buildings, equipment, machinery, fencing, and breeding stock)
2. If the business has a loan, two important parts must be accounted for when creating a cash flow budget.

- Principal payments (payments toward the money borrowed) are NOT a business expense but are a use of CASH.
- Interest payments (payments toward the money a bank charges to use the loaned money) are both a business expense and a use of CASH.

Use the information below to develop a cash flow budget for a corn enterprise (per acre) using Table 1 or Excel[®] if you have computer access.

Expected corn yield = 100 bushel per acre.

Expected corn price = \$3.40 per bushel.

Production costs (\$ per acre)

<i>Seed</i>	<i>\$62.00</i>
<i>Fertilizer</i>	<i>\$33.00</i>
<i>Pesticides</i>	<i>\$23.00</i>
<i>Crop insurance</i>	<i>\$ 8.00</i>
<i>Labor</i>	<i>\$10.00</i>
<i>Fuel, oil, and lube</i>	<i>\$58.00</i>
<i>Rent</i>	<i>\$30.00</i>
<i>Repairs</i>	<i>\$ 5.00</i>

Fixed costs (\$ per acre)

<i>Depreciation</i>	<i>\$24.00</i>
<i>Interest</i>	<i>\$16.00</i>
<i>Taxes</i>	<i>\$ 4.00</i>

Other data to consider:

- *An operating note will be taken out to cover cash expenses*
 - *Interest rate on the operating note will be 7% or a total of \$5.34 per acre for the purpose of this activity*
- *Corn will be planted in April and harvested in November*
- *Assume a \$0 beginning cash balance*

Table 1. Cash Flow Budget Worksheet	
Sources of cash	
Total sources of cash	(A)
Uses of cash	
Total uses of cash	(B)
Net cash surplus of deficit	(A-B)

Explain in complete sentence(s) what the cash flow budget in Table 1 means to the financial health of a business.

Student Reflection

1. Why are cash flow budgets important for a running a business?
2. Provide an example of a non-cash expense that you would not include in a cash flow budget.
3. Why do you think a bank would want to have a cash flow budget when deciding to loan money?