Book Smart

Using Benchmarking and Performance Indicators for Better Bottom-Line Management

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Real Life, Too
Real Life, Too

SEPE FARM, LLC
Local, Natural Connecticut Grown Lamb and Woolen Products
The Starting Line

• You understand your financials!

• They’re in good shape:
  - Accounts reconcile
  - Accurate balance sheet
  - Accrual accounting (or adjustments)

• You want to work ON your business (not just in it)
The Starting Line

- Common chart of accounts

Go to: Foodhub.info -> click “Finances”
Financial Fundamentals

Go to “foodhub.info”
Click “Finances”

- **Part 1: Introduction and the Common Chart of Accounts**
  - View the recording of this webinar

- **Part 2: Balance Sheet**
  - View the recording of this webinar
  - View the recording of the office hours for part 2

- **Part 3: Income Statement** (AKA Profit and Loss Statement)
  - View the recording of this webinar
  - View the recording of the office hours for part 3

- **Part 4: Cash Flow Statement**
  - View the recording of this webinar
  - View the recording of the office hours for part 4

- **Part 5: Putting it all together** - Managing Your Business Using Finances
  - View the recording of this webinar
  - View the recording of the office hours for part 5
Typical Income Statement

Sales - Expenses = Profit

Sales
- Cost of:
  - Goods Sold
  - Production
  - Overhead Expenses

Gross Margin
- Overhead Expenses = Profit
Apples to Apples

• Similar formats

• Common accounting
  – Is everything in the same place?

• Evaluate on a percent of sales
A word about profits

• Doesn’t matter what your business structure is. If you want to be a resilient mission-driven organization, then you need to generate profit.

• Not for profit is a tax status, not a business model.
From the Bottom Up...

• What does the bottom line tell you?

• Work up by group
  – Overhead
  – Cost of Sales
  – Cost of Production/Cost of Goods Sold
  – Sales
What if...

- **Overhead** is high?
- **Overhead** is low?

Food Hub Benchmark: 16.28%
What if...

• Gross Margin is high?

• Gross Margin is low?

Food Hub Benchmark: 14.49%
What if...

- Cost of Sales is high?
- Cost of Sales is low?

Food Hub Benchmark: 13.56%
What if...

- **Cost of Goods/Production is high?**
- **Cost of Goods/Production is low?**

Food Hub Benchmark: 71.95%
Efficiency Management: Analyzing Your Labor Resources

• Why?
  – Highest or second highest expense
  – Manage cost and time compared to productivity standard

• Measure productivity based on time
  – Standard unit of time
  – Units produced per hour/day/week etc.
Benchmarking Labor

What are the actual costs?

WAGES

... and ?
Key Components

• Labor Costs: Fully Loaded
  • Wages
  • FICA & Medicare
  • Health Insurance
  • Workers Compensation
  • Unemployment Insurance
  • Retirement Plans
  • Housing
  • Other Miscellaneous Benefits
Standard Unit of Labor: Worker Equivalents (aka FTE)

- Used to calculate output efficiency

- Process to calculate a worker equivalent
  - Set a standard for average work week
  - Add up all hours worked and divide by standard

\[
\text{51 weeks a year} \times \text{40 hours a week} = 2,040 \text{ hours}
\]
Measure Labor Efficiency

• Track changes in output over time
  – By day, week, year
  – By divisions

• Track changes in cost over time
  – Compare labor cost increase to gross sales increase

What gets measured gets managed.
Efficiency and Productivity Management

Our Sample Food Hub

- Labor Hours 13,364
- Labor Dollars $421,824
- Sales $2,653,642
- 40 hour workweek is typical

Calculate the following:

- Worker equivalents
- Labor expense per worker equivalent
- Labor cost as a percent of sales
- Sales per worker equivalent
Our Sample Food Hub

- Labor Hours          13,364
- Labor Dollars        $421,824
- Sales               $2,653,642
- 40 hour workweek is typical

Calculate Worker Equivalents:

13,364 hours ÷ 2,040 hours per year = 6.55 worker equivalents
Our Sample Food Hub

- Labor Hours: 13,364
- Labor Dollars: $421,824
- Sales: $2,653,642
- 40 hour workweek is typical

Calculate Labor Cost per Worker Equiv:

$421,824 \div 6.55 \text{ worker equivalents} = $64,400 \text{ cost per worker equivalent}
Our Sample Food Hub

- Labor Hours 13,364
- Labor Dollars $421,824
- Sales $2,653,642
- 40 hour workweek is typical

Calculate Labor Cost as a Percent of Sales:

$421,824 for labor ÷ $2,653,642 in sales = 15.89% of sales
Our Sample Food Hub

- Labor Hours 13,364
- Labor Dollars $421,824
- Sales $2,653,642
- 40 hour workweek is typical

Calculate Sales per Worker Equivalent:

$2,653,642 in sales ÷ 6.55 worker equivalents = $405,136 sales per worker equivalent
Efficiency and Productivity Management

Our Sample Food Hub

- Labor Hours 13,364
- Labor Dollars $421,824
- Sales $2,653,642
- 40 hour workweek is typical

Calculate the following:

- Worker equivalents 6.55
- Labor expense per worker equivalent $64,400
- Labor cost as a percent of sales 15.89%
- Sales per worker equivalent $405,136
What if we knew...

• By Department:
  Sales of *produce* compared to the cost of *produce*?
  Sales of *salsa* compared to the cost of *salsa*?
  Sales of *pickled products* compared to the cost of *pickled products*?

*This works universally!*

*purchased - produced - processed - brokered*

• Why?
  – Figure % gross margin
  – Is the product contributing to overhead and profit?
  – Is the product carrying its own weight?
  – Decide on future allocations
### What should we do next?

<table>
<thead>
<tr>
<th></th>
<th>Sales</th>
<th>Less COGS (including production labor!)</th>
<th>Gross Margin</th>
</tr>
</thead>
<tbody>
<tr>
<td>Produce (resale)</td>
<td>$45,000</td>
<td>$27,000</td>
<td>$18,000 (40%)</td>
</tr>
<tr>
<td>Produce (homegrown)</td>
<td>$90,000</td>
<td>$23,000 - $45,000</td>
<td>$22,000 (24%)</td>
</tr>
<tr>
<td>Pumpkins</td>
<td>$60,000</td>
<td>$23,000 - $15,000</td>
<td>$22,000 (37%)</td>
</tr>
</tbody>
</table>

Sales – COGS = Gross Margin  
Gross Margin / Sales = GM%
Beware of...

• Not enough detail
  - “Sales” as a category

• Mixed dimensions
  - Farmers’ Market Income (WHERE)
  - Wholesale (HOW)
  - Greens (WHAT)

• Offsets
  - Discounts - what was discounted?
  - Credits/Returns – what was returned?
  - Reimbursements – reduce your true cost (are not income)
What’s a healthy net worth?

Net Worth % = \[
\frac{\text{Equity}}{\text{Total Assets}} \times 100
\]

- Kohls’ Traffic Lights
  Scoring for next move:

- **Red** = STOP  Net Worth < 40%
- **Yellow** = CAUTION  40% < Net Worth < 70%
- **Green** = GO  Net Worth > 70%
Balance Sheet: What does it tell you?

• Liquidity
  – Current Ratio
    Current Assets ÷ Current Liabilities
  – Working Capital
    Current Assets – Current Liabilities

Food Hub Benchmark: 2.39:1
## G & E’s Food Hub

**Balance Sheets - Fair Market Value**

As of December 31, 2017 and December 31, 2016

<table>
<thead>
<tr>
<th></th>
<th></th>
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<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current Assets</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>31,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts Receivable</td>
<td>8,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Inventory</td>
<td>139,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Supplies</td>
<td>41,500</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Prepaid Expenses</td>
<td>5,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other Current Assets</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL CURRENT ASSETS</strong></td>
<td><strong>224,500</strong></td>
<td></td>
<td><strong>220,000</strong></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>2017</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current Liabilities</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts Payable</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>Accrued Expenses</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>Operating Loan</td>
<td>140,000</td>
<td></td>
</tr>
<tr>
<td>Current Portion of IT Loans</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>Current Portion of LT Loans</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL CURRENT LIABILITIES</strong></td>
<td><strong>220,000</strong></td>
<td></td>
</tr>
</tbody>
</table>

**Current Ratio:** \( \frac{Current\ Assets}{Current\ Liabilities} : 1 \)

*2016: 1.02:1*

**Working Capital:** \( Current\ Assets - Current\ Liabilities \)

*2016: 4,500*
# G & E’s Food Hub

Balance Sheets - Fair Market Value

As of December 31, 2017 and December 31, 2016

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<tbody>
<tr>
<td><strong>Current Assets</strong></td>
<td></td>
<td></td>
<td><strong>Current Liabilities</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>58,742</td>
<td>31,000</td>
<td>Accounts Payable</td>
<td>8,758</td>
<td>15,000</td>
</tr>
<tr>
<td>Accounts Receivable</td>
<td>65,412</td>
<td>8,000</td>
<td>Accrued Expenses</td>
<td>10,000</td>
<td>0</td>
</tr>
<tr>
<td>Inventory</td>
<td>190,578</td>
<td>139,000</td>
<td>Operating Loan</td>
<td>100,000</td>
<td>140,000</td>
</tr>
<tr>
<td>Supplies</td>
<td>46,000</td>
<td>41,500</td>
<td>Current Portion of IT Loans</td>
<td>8,000</td>
<td>15,000</td>
</tr>
<tr>
<td>Prepaid Expenses</td>
<td>6,500</td>
<td>5,000</td>
<td>Current Portion of LT Loans</td>
<td>50,000</td>
<td>50,000</td>
</tr>
<tr>
<td>Other Current Assets</td>
<td>3,076</td>
<td>-</td>
<td><strong>TOTAL CURRENT ASSETS</strong></td>
<td>370,308</td>
<td>224,500</td>
</tr>
</tbody>
</table>

**Total Current Liabilities**

<table>
<thead>
<tr>
<th></th>
<th>2017</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accounts Payable</td>
<td>8,758</td>
<td>15,000</td>
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<tr>
<td>Accrued Expenses</td>
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**TOTAL CURRENT LIABILITIES**

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<tr>
<th></th>
<th>2017</th>
<th>2016</th>
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<tbody>
<tr>
<td><strong>Current Ratio</strong>:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current Assets ÷ Current Liabilities :1</td>
<td>2016: 1.02:1</td>
<td>2017: 2.09:1</td>
</tr>
</tbody>
</table>

**Working Capital**: Current Assets – Current Liabilities

<table>
<thead>
<tr>
<th></th>
<th>2016</th>
<th>2017</th>
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<tbody>
<tr>
<td></td>
<td>4,500</td>
<td>193,550</td>
</tr>
</tbody>
</table>

*Note: The current ratio and working capital have improved significantly in 2017 compared to 2016.*
Adequate working capital depends on:

- Commodity
- How often income is received
- How often are payments made to vendors
- Stability of prices and COGS
- Ability for business to withstand price fluctuations
- Surprises
- Guideline: >25% of total expenses
This works

• For every kind of business

• Need to know:
  – Who you are comparing to
  – Basis for comparison
  – The common denominator (aka unit of measure)
Cash Flow and Profit are not the same thing

• Forecasting cash flow
• - know A/R and A/P days

• When you’re broke, the stakes are low

• When you’re growing fast, you have momentum, you need the cash
Resources

• Financial Fundamentals for Food Hubs
• Counting Values
• Food Hub Manager’s Guide to Finances

Food Hub Benchmarking 2018!!
farmcrediteast.com/foodhubs
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(202) 879-0840

- Profitability Analysis
- Profitability Enhancement
- Benchmarking
- Margin Improvement
- Records for Management
- Records Training

- Strategic Business Planning
- Succession Planning
- Transition Planning
- Expansion Planning