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### **Business IQ**

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Financial literacy will be the deal breaker in an economic environment with tight margins and extreme volatility. Managers who have a business mindset and high business IQ will be the difference makers for profitability and cash flow over the next decade. These were the sentiments of the agriculture bankers and agribusiness lenders at the most recent National Agricultural Bankers Conference in Omaha, Nebraska.

Where do you stand on the business IQ spectrum? Let's draw upon a scorecard that can assess business acumen, but more importantly raise critical questions that create crucial conversations with your family members and lenders to improve your bottom line performance.

Based on a request from Royal Bank of Canada, the business IQ scorecard was developed to place more emphasis on management in the credit assessment process. The scorecard is a combination of decades of engagement with thought leaders, academics, and practitioners involved in research, extension, and consultation of business management on farms and ranches.

Fifteen areas were identified as characteristics that place profitable businesses above their peers who represent average or below average performance. A score of one to four points is used in each one of the areas. You may receive one point if you have no idea, have never done it, or the item in question is nonexistent. Since everyone gets a trophy in today's society, receiving one point is a quick and dirty answer! However, one banker indicated that if you score one point, then at least you may recognize that there is an issue or an opportunity for improvement.

First, do you know your cost production and is it written or stored in your head? Knowing your cost of production is one of the basic business principles. However, less than half of businesses have a quantifiable answer. To examine the question further, if your business has multiple enterprises, do you know the cost of production for each segment? This allows you to allocate capital, labor, and time where you can get the "biggest bang for the buck" of deployed resources.



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Next on the list is the old-fashioned goal setting process. Written goals provide a map of where you want your business to go in the short-term and long-term. Your goals should be defined by their term of completion with short-term goals being completed within one year and long-term goals stretching three to five years. Applied research finds that less than one out of five agriculture producers have written goals.

What is your record keeping system? Do you operate the business from your Schedule F tax form with the goal to minimize taxes through revenue and cost manipulation? Do you utilize an accrual adjusted income statement when making business decisions? Numerous academic research studies have found large variations between cash and accrual income statements.

Managers with a high business IQ will prepare the basic cash flow statement monthly or quarterly. This statement is a high priority management item in a high volatility, low margin economic environment. The key is to compare projected and actual results so that adjustments can be made throughout the year. Financial statements that test key variables such as production, price, cost, and interest rates provide a critical pathway of possible outcomes that take some of the emotion out of a highly charged, intense type of environment.

Next, do you have a dashboard of key financial ratios and their benchmarks to track your performance over time and compare your results to your peers? Remember, financial ratios only identify symptoms of a problem, not the root cause or the possible opportunities. Are you willing to work with an advisory team including professionals such as a farm management instructor, agriculture lender, crop or livestock consultant, marketing specialist, or a financial advisor? Another set of eyes provides perspective and confirms or challenges the status quo.

Marketing and risk management plans that are executed and monitored periodically are very critical to the bottom line. Risk management encompasses insurances, compliance, and all production and business management practices.

Does your business and family live within its means? Family living budgets are just as important as farm budgets.

You often hear athletes say that they are attempting to get a little better each day. The same can be applied to farm business management strategy. Each of you must identify your priorities to improve the financial or business management situation. Also, what is your human resource acumen and your ability to work with people? These soft skills will be very critical in the future.

All businesses are in a state of transition, regardless of the business cycle. Has a plan been developed for the transfer of skill sets or replenishing areas of the business should a change occur with the stakeholders of the business?

Education will be a key component of successful businesses. The ability to attend and engage in events that improve business and personal performance must be a high priority.



Finally, there is a saying to “hire for attitude, rather than aptitude.” The same goes for all managers, owners, and stakeholders of the business. The difference between a proactive, reactive, or indifferent attitude can be a big difference in business.

Now that you have completed the assessment, a good score is 32 points or above. A peak performing business often will score 40 points or more.

How do you apply this to your business if you have multiple partners or family members?

Have each stakeholder complete the assessment and then contrast and compare results.

Involve your lender and farm management instructor when examining the outcomes.

After completing the assessment, identify strategies to build upon your strengths and outline areas for improvement. Are you willing to take a little time to complete the assessment and then do something about it? Of course, that is all up to you. The Business IQ assessment tool is below.

## Business IQ: Management Factors

### Critical Questions for Crucial Conversations

Customer Checklist	Green (3-4 points*)	Yellow (2 points)	Red (1 point)
1. Knows cost of production	Written	In head	No idea
2. Knows cost of production by enterprise	Written	In head	No idea
3. Goals- business, family & personal	Written	In head	No idea
4. Record keeping system	Accrual	Schedule F (one & done)	No idea
5. Projected cash flow	Written	In head	No idea
6. Sensitivity analysis	Written	In head	No idea
7. Understand financial ratios, break evens	Written	In head	No idea
8. Work with advisory team and lender	Yes	Sometimes	Never
9. Marketing plan written and executed	Yes	Sometimes	Never
10. Risk management plan executed	Yes	Sometimes	Never
11. Modest lifestyle habits, family living budget	Yes	Sometimes	Non existent
12. Written plan for improvement executed & strong people management	Yes	Sometimes	Non existent
13. Transition plan/Business Owner plan	Yes	Working on plan	Non existent/controversy
14. Educational seminars/courses	Yes	Sometimes	Never attend
15. Attitude	Proactive	Reactive	Indifferent

**\*Extra Points:**

- Progressive Business** may receive 4 points for #2,6,7,8,14
- Struggling Business attempting turnaround** may receive 4 points for #3,5,8,11,12

Score	Overall Analysis
35-50	Strong management rating & viability
20-34	Moderate risk & viability; will most likely show previous refinancing
<20	High risk & lack of long term viability





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