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Meeting Cash Flow Needs

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Cornhusker Economics

Cooperative Extension

Institute of Agriculture & Natural Resources
Department of Agricultural Economics
University of Nebraska – Lincoln

Meeting Cash Flow Needs

Market Report	Yr Ago	4 Wks Ago	11/6/98
Livestock and Products, Average Prices for Week Ending			
Slaughter Steers, Ch. 204, 1100-1300 lb Omaha, cwt.	$66.94	$56.25	$59.50
Feeder Steers, Med. Frame, 600-650 lb Dodge City, KS, cwt.	77.72	68.50	69.50
Carcass Price, Ch. 1-3, 550-700 lb Cent. US, Equiv. Index Value, cwt.	101.22	90.65	97.77
Hogs, US 1-2, 220-230 lb Omaha, cwt.	45.20	29.00	20.08
Feeder Pigs, US 1-2, 40-45 lb Omaha, hd.	*	*	*
Vacuum Packed Pork Loins, Wholesale, 13-19 lb, 1/4" Trim, Cent. US, cwt.	89.80	97.10	81.30
Slaughter Lambs, Ch. & Pr., 115-125 lb Sioux Falls, SD, cwt.	79.38	65.50	58.40
Carcass Lambs, Ch. & Pr., 1-4, 55-65 lb FOB Midwest, cwt.	159.50	158.00	135.00
Crops, Cash Truck Prices for Date Shown			
Wheat, No. 1, H.W. Omaha, bu.	3.56	2.85	3.32
Corn, No. 2, Yellow Omaha, bu.	2.60	1.79	1.90
Soybeans, No. 1, Yellow Chicago, bu.	7.36	5.42	5.43
Grain Sorghum, No. 2, Yellow Kansas City, cwt.	4.40	3.15	3.33
Oats, No. 2, Heavy Omaha, bu.	*	*	*
Hay, First Day of Week Pile Prices			
Alfalfa, Sm. Square, RFV 150 or better Platte Valley, ton.	*	*	*
Alfalfa, Lg. Round, Good Northeast Nebraska, ton.	92.50	58.00	60.00
Prairie, Sm. Square, Good Northeast Nebraska, ton.	117.50	70.00	70.00

* No market.

In the March 11, 1998 issue of this newsletter we discussed how projected cash requirements for the year could be distributed between enterprises. The objectives of that discussion were to arrive at 1) a budgeted cash requirement on a per acre basis to help determine crop insurance needs, and 2) a target price for each enterprise to help in pricing decisions. We suggested, however, that prioritization of cash requirements may be needed because yield and price protection may not be available at those levels or may cost more than you are willing to spend. The low prices we are currently facing increases this possibility.

Here we will illustrate a procedure that involves a review of cash commitments considering possible adjustments and prioritization. We will then total the cash commitments by priority level, which can then be used to determine new cash needs per enterprise unit (per acre or per head) and per sales unit (price per bushel or per pound), as we did in the March 11 newsletter. We will also illustrate here how these priority needs might be met in total without making any enterprise assignments.

In prioritizing cash needs it will be helpful to have a listing that provides sufficient detail to split out each category by priority. For example, consider three priority levels as follows:

Priority I *Must* meet

Priority II Would like to cover, but *could be* deferred

Priority III How additional cash would be used in a *good* year.

With this approach it will be helpful to have total debt payments, for example, listed for each obligation and split between interest and principal. The number of priority

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levels is arbitrary of course. You may want to use two levels. After the list of all cash needs has been completed it may be useful to review each item for:

1. Adequacy (e.g., repairs realistic)?
2. Possible reduction (e.g., cost cutting).
3. Possible deferral (e.g., restructure current debt payments to long-term to defer principal payments).

Adjust budgeted cash commitments as appropriate, i.e., correct budgeted amount to reflect improved estimates and any restructuring. Then prioritize each final budgeted amount into the three levels.

The cash needs can then be distributed by priority level, totaled and accumulated so that cash needs are summarized as Priority I, Priority I and II, and Total (Priority I, II and III).

Examples of prioritization are:

	Priority I	**Priority II**	**Priority III**
Family Living	Groceries, insurance, utilities, gas	Vacation, trade car	Add to savings
Debt Payments	Interest only, increase operating loan carryover	Principal	Prepay principal
Capital Purchases and Repairs	Those necessary to maintain business	Those that could be deferred another year	Those budgeted, but not included in I or II

These three levels of cash needs can then be distributed between enterprises to determine per acre cash needs, for example, to provide a guide for selecting the level of multi-peril insurance or assuming a yield level to provide target prices at three levels.

Alternatively the three cash need totals by priority level could be compared to total cash inflows that can be "insured" or "assured" through government payments, off farm employment, crop insurance and production contracts. Consider the following projected cash needs:

	Priority		**I**	**II**	**III**
1.	Debt Payments $20,000 Principal, $30,000 Interest		$ 30,000	$ 20,000	$ 10,000
2.	Taxes		$ 8,000		
3.	Insurance		$ 1,500		
4.	Other Cash Expenses		$ 1,000		
5.	Capital Purchases (portion to be from cash)			$ 6,000	$ 20,000
6.	Family Living		$ 25,000	$ 5,000	$ 5,000
7.	Materials and Services (Livestock and Crops)		$111,300		
			$176,800	$ 31,000	$ 35,000
		Accumulated	$176,800	$207,800	$242,800

Now consider projected other cash receipts:

8.	Sale of Culls and Miscellaneous Income	$9,500
9.	Nonfarm Income, Cash Transfers	$20,000
10.	Government Payments	$15,300
11.	**Total**	**$44,800**

Subtracting these relatively assured projected cash receipts from our cash needs priorities results in balances of:

	Priority	I	II	III
12.	Net Cash Need	$132,000	$207,800	$242,800

These needs could then be allocated to enterprises by first projecting revenues:

		Corn	Cow-Calf
13.	Number	500 acre	100 head
14.	Expected Production	150 bu.	400 lb.
15.	Projected Sale Price	$2.40/bu.	$0.80/lb.
16.	Projected Value of Production	$180,000	$32,000
17.	Share of Total	85%	15%

Note that these percentages are different than calculated in the March 11 newsletter since they were previously calculated net of production expenses, and here we have included production expenses in our net cash needs.

We can calculate per acre needs and per unit needs as follows:

	Priority	I	II	III
12.	Net Cash Need	$132,000	$207,800	$242,800
18.	Corn Share (Line 17 x Line 12)	$112,200	$176,630	$206,380
19.	Per Acre (Line 18/Line 13)	$224	$353	$413
20.	Per Bushel (Line 19/Line 14)	$1.50	$2.36	$2.75

Alternatively, consider multi-peril crop insurance that could be purchased at the 65% level at a $2.20 price election and the calves could be hedged at $70/cwt. An "insured" level of cash income could then be calculated as:

500 acres	x	150 bu.	x	65%	x	$2.20/bu.	=	$107,250
100 head	x	400 lbs.	x	0.70/lb.			=	$ 28,000
								$135,250

This "insured" level of cash income exceeds our Level I net cash need (Line 12), and probably enough to pay the insurance premium, the broker's fee and margin interest on the hedge. If we wanted more protection we could consider insurance at the 75% level which, however, would fall short of our Level II cash need.

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