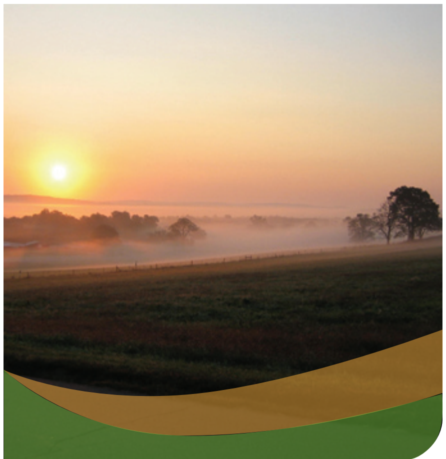

Connecticut
Farm Risk Management and Crop Insurance Program

Managing Financial Risk

INTRODUCTION

FINANCIAL RISK IS ASSOCIATED WITH YOUR ABILITY TO BOTH SAFEGUARD AND EXPAND YOUR FARM'S EQUITY WHILE AT THE SAME TIME PROMPTLY FULFILLING ALL CASH FLOW REQUIREMENTS AND ENSURING LIQUIDITY. FURTHERMORE, IT IS IMPORTANT TO RECOGNIZE THE RISK OF INFLATION AND FLUCTUATIONS IN INTEREST RATES. THE KEY TO MANAGING THIS FORM OF RISK IS TO KEEP UPDATED RECORDS AND CLOSELY MONITOR ALL FINANCIAL TRANSACTIONS.

Record Keeping

Regardless of your farm's size, effective record keeping is imperative for you to understand potential financial risks as well as for your farm to successfully operate. Essential records include balance sheets, income statements, statement of owner's equity, and projected and annual cash flows. According to the USDA, not only will these records detail your farm's history, but they will also provide necessary data to measure annual financial performance.

Equity

Many farm owners share the ultimate goal of building equity or the net worth of their farm businesses. Having equity is essential in maintaining the life of your farm. There are many ways that this can be accomplished. Net income that is not being spent on income tax or family living expenses can be used to build equity, which can in turn generate future income, provide a source of retirement income, or left as inheritances to heirs. Another important function of equity is for the acquisition of loans. Anytime you want to expand your business or wish to take out a loan to cover expenses, your creditor is going to want proof that you can pay back the loan for which you are applying. For this reason, a statement of owner's equity is important to keep with your financial records.

Liquidity

The availability of funds to operate the farm is referred to as liquidity. Maintaining liquidity is important to make certain that there is adequate cash flow to finance operations. Sufficient cash flow is essential in protecting your farm during potential financial setbacks. Liquidity can be measured by working capital and current ratio. Working capital is the amount of money available for running the farm and is calculated as the difference between current assets and current liabilities. The current ratio measures the relationship between current assets and the farm liabilities that are due within the same period. There are several ways to ensure that you have proper cash flows by building liquidity, including leasing assets, cutting back on living expenses, and exploiting insurance programs.

Crop Insurance

A significant way to reduce the financial risk associated with farming is for you to purchase crop insurance, which is subsidized and regulated by the USDA Risk Management Agency. On the condition that an adequate amount of protection is purchased, crop insurance's purpose is to help farmers withstand and recover from disasters. It can also provide liquid security that can be used for loan security. Regardless of the fact that insurance is renewable each year, you should still do an annual evaluation to determine whether or not you have an appropriate level of coverage. It is recommended that you consult a professional in order to ensure that you are adequately covered under the proper types of insurance.

Living Expenses

There are many costs associated with everyday living. To manage financial risks, family living expenses must be

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effectively controlled. Outlining and adhering to a budget that includes all of your living costs is the best place to start. Once you have established your weekly, monthly and yearly family expenses, you must ensure that you can fulfill these financial obligations. The USDA suggests that it may be necessary for family members to seek outside employment to not only generate extra funds, but also to reduce the need to liquidate farm assets to meet family living expenses.

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CFRM-FS-3. Managing Financial Risk. Prepared by Elizabeth Olney*, Brianne Neptin* and Marilyn Altobello** Dept. of Agricultural and Resource Economics, University of Connecticut, Storrs. 2008.

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