FAMILY FARMS LLC

5 Measures of Financial Efficiency

How Efficient is Your Operation?

Efficiency is getting more output from the same resources or getting the same output from fewer resources. There are 5 efficiency ratios used to measure production or financial efficiency, or a combination of both.

For financial efficiency, the primary measure is the asset turnover ratio.

$$ATR = \frac{GFR}{ATFA}$$

Asset Turnover Ratio = **Gross Farm Revenues** divided by **Average Total Farm Assets**

60%

Asset Turnover Ratio measures how efficiently farm assets are being used to generate revenue. An asset turnover ratio of

60% or higher

is considered healthy/efficient use of assets. Generally, the higher the ratio, the more efficiently assets are being used to generate revenue.

$$OER = \frac{TFOE}{GFR}$$

Operating Expense Ratio = **Total Farm Operating Expenses** divided by **Gross Farm Revenues**

For more detailed analysis and for benchmarking purposes, the **Operating Expense Ratio** can be broken down into individual expense categories as a percent of gross revenues, e.g., chemicals, crop insurance, seed, equipment cost, etc.

$$DER = \frac{DE}{GFR}$$

Depreciation Expense Ratio = **Total Farm Interest Expense** divided by **Gross Farm Revenues**

The **Depreciation Expense Ratio** will vary widely between operations because of the different depreciation methods used and the difference in the amount of depreciable assets used in production.

$$IER = \frac{TFIE}{GFR}$$

Interest Expense Ratio = **Total Farm Interest Expense** divided by **Gross Farm Revenues**

20%

Generally, the **Interest Expense Ratio** needs to be

less than 20%

to allow a profitable operation. If it exceeds 20%, it may indicate the operation is carrying a heavier debt load than it can sustain.

$$NFI \text{ (from Operations Ratio)} = \frac{NFI \text{ (from Operations Ratio)}}{GFR}$$

Net Farm Income from Operations Ratio = **Net Farm Income from Operations Ratio** divided by **Gross Farm Revenues**

How High Are Your Financial Ratios?

Agricultural producers in the lower end of the ratio goals will obviously feel financial stress first as margins tighten. Agricultural producers with lower cost and high financial efficiencies tend to have the staying power to weather the downturns.

Financial ratios measure your progress over time, to make sure you're meeting your lender's requirements and to benchmark yourself against your peers.

If you need more help, there are expert consultants at **FamilyFarms Group**

Our goal is not to take over in any of these areas, but to help you implement improved managing practices. Contact us to learn about other ways to improve your operation.

CONTACT US!