FACT SHEET:
BUSINESS PERFORMANCE MEASURES

Knowing the "Five C's" is a good place to start (see Ag Lending 101) but farmers with more complicated business plans might find the "Sweet Sixteen" to be more helpful. The "Sweet Sixteen" are ratios and calculations used by bankers and lenders to measure business performance. Below are some of the **key** ratios and calculations defining Liquidity, Solvency, Profitability, Repayment Capacity, and Financial Efficiency. Find the full list of ratios and calculations in **The Farmer's Guide to Agricultural Credit http://rafiusa.org/blog/the-farmers-guide-to-agricultural-credit/**

Key "Sweet Sixteen" Ratios and Calculations

RATIO	EXPLANATION
Liquidity	
Current Ratio: Calculated as (total current farm assets) ÷ (total current farm liabilities)	This measure of liquidity reflects the extend to which current farm assets, if sold tomorrow, could pay off current farm liabilities.
Working Capital: Calculated as (total current farm assets) – (total current farm liabilities)	This measure represents the short-term operating capital available from within the business.
Solvency	
Debt-to-Asset Ratio: Calculated as (total current farm liabilities) ÷ (total farm assets)	This represents the bank's share of your business. A higher ratio is an indicator of greater financial risk and lower borrowing capacity.

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Key “Sweet Sixteen” Ratios and Calculations

RATIO	EXPLANATION
Profitability	
Rate of Return on Equity: Calculated as [(net farm income) – (value of operator labor and management)] ÷ (average farm net worth)	This measure represents the “interest” rate being earned by your investment in the farm. This return can be compared to the return on your investments if equity were invested somewhere else, outside the business.
Operating Profit Margin: Calculated as (return on farm assets) ÷ (value of farm production), where return on farm assets equals (net farm income from operation) + (farm interest expense) – (opportunity return to labor and management)	This measure of profitability shows the operating efficiency of the business. Low expenses relative to the value of farm production result in a healthy operating profit margin.
Repayment Capacity	
Term Debt Coverage Ratio: Calculated as [(net farm operating income) + (net nonfarm income) + (depreciation) + (scheduled interest on term debt and capital leases) – (family living and taxes paid)] ÷ (scheduled principal and interest payments on term debt and capital leases)	This measure of repayment capacity tells whether the business produced enough cash to cover all intermediate and long-term debt payments.
Financial Efficiency	
Operating Expense Ratio: Calculated as the value of [(total farm operating expenses)– (depreciation) – (farm interest)] ÷ (gross farm revenue)	This measure reflects the proportion of farm revenues used to pay operating expenses, not including principal or interest.

FOR MORE INFORMATION, SEE THE FARMER’S GUIDE TO AGRICULTURAL CREDIT
http://rafiusa.org/blog/the-farmers-guide-to-agricultural-credit/