# Financial Analysis From A Lender's Perspective

**Editor's Note: This is the fifth of a seven part series to explain how Farm Credit analyzes farm and ranch businesses. A different aspect of financial analysis is addressed in each issue.**

## Analyzing loan repayment — how we estimate future crop and livestock income

he most important factor in deciding to loan money is a reliable analysis showing the loan can be repaid from future income generated by the farm or ranch operation. Since that analysis includes income from crops or livestock not yet grown or marketed, it's necessary to make some assumptions to project future income. This analysis involves projecting both yields and prices.

### *Yields*

The primary source of information for a lender's projections on crop or livestock yields is the operator's records for the last few years. In addition, the lender must understand the operator's production plans for the future as well as current conditions, such as drought affecting the area. Future projections for yields will be consistent with the operator's historical yields, unless other factors clearly support increased or reduced yields.

### *Prices*

Price and yield projections depend on the terms of the loans being analyzed for repayment.

**Near-term prices and yields are** used to project repayment for annual operating loans. A near-term price or yield is the price or output expected over the budget or marketing cycle. These figures reflect the status of the industry and area (surplus or shortage, drought or wet conditions, etc.) as well as the producer's ability to consistently obtain above or below average prices and yields. Projecting repayment with near-term prices and yields is a reliable method to analyze expected income and changes in working capital over the next operating cycle.

**Normal prices and yields** are used to project repayment on intermediate- and long-term loans. A normal price is the price which the market is not expected to fall below for a sustained period during the next three to five years. Normal yields are minimum yields which the producer is expected to produce over the three- to five-year period. Normal prices and yields are used to determine the customer's ability to service all debts over the life of the loan. They are also used when:

- Expansion or changes in an operation make use of information from the operator's records inappropriate.
- A new operator or enterprise without history is being financed.
- The operator's records reflect periods considered unusual, either above or below average for reasons such as weather, health, or other uncontrollable circumstances.

### *Lender projections*

To determine near-term or normal prices, a lender must understand the history and project the future of commodities produced by its customers. The lender must also understand individual customers since the ability to both produce and market commodities can vary greatly among producers.

Analyzing loan repayment is not an exact science but an art that is most correct when reliable records are combined with an understanding of the customer's operation and the industry.

**Next week we will look at net earnings.**

# Elliott Receives Advising Award

UNIVERSITY PARK (Centre Co.) — Dr. Herschel A. Elliott, professor of agricultural engineering and coordinator of the environmental resource management program at Penn State, has received the 1993 College of Agricultural Sciences Alumni Society's Excellence in Academic Advising Award.

Elliott will receive the award at the College of Agricultural Sciences 1993 Spring Commencement on Saturday, May 15, at 9 a.m. in Eisenhower Auditorium on Penn State's University Park Campus.

The award recognizes faculty with outstanding skills in academic advising, career planning, and personal counseling. Advisers in the college are nominated by alumni, faculty, students, and administrators.

"Dr. Elliott exemplifies what an adviser should be," said colleague Dr. James R. Pratt, assistant professor of aquatic ecology. "He is available to students, he is aware of career needs and the state of the job market, and he has the experience and caring attitude needed to help students through difficult situations."

As coordinator of the interdisciplinary environmental resource management (ERM) program, Elliott is the first contact for students entering the college's largest program. He provides transitional counseling, often to students in search of career goals. Elliott also advises the student ERM club and coordinates internships for ERM students.

"Beyond the mechanics of course selection and scheduling, I derive great satsifaction from counseling students at the crossroads, helping them to define and choose among various paths," Elliott said.

Because ERM is an interdisciplinary program, Elliott oversees advisers and faculty in several departments. He works to assure that each adviser has the most current information needed by students. He also bears the largest share of advising responsibility in the ERM program, advising more than 150 students.

"To me, Dr. Elliott personifies the ideal academic adviser," said one advisee. "He has been a friend as well as an academic adviser and career counselor. He has helped me on numerous occasions because of his availability and willingness to talk."

Another advisee said, "Dr. Elliott attempts to develop the whole student. This kind of advising is remarkable when one considers all the responsibilities placed on the coordinator of an ever-changing and growing program."

Elliott joined Penn State as an associate professor in 1984 and became a full professor in 1990. Before joining Penn State he was an associate professor of agricultural engineering at the University of Delaware. Elliott is a registered professional engineer and a member of numerous honor societies and professional associations, including Tau Beta Pi.