

Lesson E1–2

Financial Management in the Horticulture Business

Unit E. Horticultural Business Management

Problem Area I. Entrepreneurship in Horticulture

Lesson 2. Financial Management in the Horticulture Business

New Mexico Content Standard:

Pathway Strand: Agribusiness Systems

Standard: II: Practice good record keeping to accomplish AFNR business objectives.

Benchmark: II-A: Prepare and maintain all files as needed to accomplish effective record keeping.

Performance Standard: 1. Identify information management systems. 2. Develop record keeping techniques and practices. 3. Keep production and agribusiness records. 4. Make record analysis.

Student Learning Objectives. Instruction in this lesson should result in students achieving the following objectives:

1. Identify the purposes for financial management.
2. Define basic financial management principles.
3. Identify the parts of a financial management plan.
4. Describe the different types of records kept in horticulture businesses.
5. Explain how to calculate the cost of products and services.

List of Resources. The following resources may be useful in teaching this lesson:

Recommended Resources. One of the following resources should be selected to accompany the lesson:

Schroeder, Charles B., et al. *Introduction to Horticulture*, Third Edition. Danville, Illinois: Interstate Publishers, Inc., 2000.

Newman, Michael E. and Walter J. Wills. *Agribusiness Management and Entrepreneurship*. Third Edition. Danville, Illinois: Interstate Publishers, Inc., 1994.

Other Resources. The following resources will be useful to students and teachers:

Ricketts, Cliff and Omri Rawlins. *Introduction to Agribusiness*. Albany, New York: Delmar Publishers, 2001.

List of Equipment, Tools, Supplies and Facilities

Writing surface
Overhead projector
Transparencies from attached masters

Terms. The following terms are presented in this lesson (shown in bold italics):

Accountant
Assets
Balance sheet
Capital
Cash flow
Cost
Equities
Expense
Fixed costs
Liabilities
Net worth
Overhead costs
Profit
Profit and loss statement
Revenue
Selling price
Transaction
Variable costs

Interest Approach. Use an interest approach that will prepare the students for the lesson. Teachers often develop approaches for their unique class and student situations. A possible approach is included here.

Ask students to consider what would happen to a business that didn't have a financial management plan. Would they be able to pay all of their bills? What would happen if their money ran out before they paid their employees? How would you feel if your boss didn't pay you for your work? Discuss student responses and continue with the lesson.

Summary of Content and Teaching Strategies

Objective 1: Identify the purposes for financial management.

Anticipated Problem: What are the purposes of financial management?

- I. For a business to remain profitable, it is important for it to have sound financial management. Businesses have written financial management plans that make it easier to determine the performance of a business.
 - A. There are two common ways for the performance of businesses to be measured. One way is to compare past and present performance of the same company. The second is to compare business performance against the performance of other businesses in the same industry.
 - B. Business performance can also be measured by comparing the performance of the business to the business' stated objectives.

Explain to students that determining a business' level of performance is similar to grading papers. Better business performance is a result of a better understanding of the customer's needs. Likewise, better performance on a homework assignment is a result of a better understanding of the lesson. Use TM: E1-2A to highlight the ways a business' performance can be checked.

Objective 2: Define basic financial management principles.

Anticipated Problem: What are examples of basic financial management principles?

- II. Running a business requires funds to pay workers, suppliers, and to pay for expenses. **Expense** is the cost of producing a product. An **accountant** is a person who is responsible for keeping track of expenses, finances, and all business transactions. A **transaction** is a business deal or an agreement. Transactions affect what is called an accounting equation. In an accounting equation, the sum of liabilities and capital equal assets.
 - A. **Liabilities** are the debts of the business. A liability is a type of equity. **Equities** are the amount something is worth beyond what is owed on it. In the end, assets should equal equity.

- B. Another form of equity is capital. **Capital** is the equity of the business owners.
- C. **Assets** are all the elements on the balance sheet that show the resources of the business. When a business generates **revenue**, increase in capital due to business transactions, the equation changes. The result of revenues minus expense is added.

At this point it may be necessary to stop and review the terminology in Objective 2. TM: E1–2B highlights most of the terminology in this section. It may be necessary to refer to the recommended texts for additional review. Continue to review until the students are comfortable with the terms.

Objective 3: Identify the parts of a financial management plan.

Anticipated Problem: What are the parts of a financial management plan?

- III. There are four main parts of a financial management plan. Important business decisions will be based on the information presented in the statement within the plan. The four parts of the plan are the cash flow analysis, profit and loss statement, balance sheet, and the source and use of funds.
 - A. **Cash flow** is the amount of money that goes in and out of a business. Analyzing this flow will help a business plan and manage debt. A cash flow statement helps a business determine when it will need to borrow money, how much money it will need to borrow, and when to pay it back.
 - B. A **profit and loss statement** is a summary of a business's income and expenses for a given period of time. To utilize a profit and loss statement it is important to compare them to past statements. In comparing the statements it is important to keep in mind any changes that have occurred that may also affect profits and losses.
 - C. A listing of a business's assets and liabilities is called a **balance sheet**. A balance sheet is a careful breakdown of what a business owns, owes, and its net worth. **Net worth** is the difference between a company's assets and liabilities, or their equity.
 - D. A list of a company's sources and uses of funds is useful in determining how much money a company needs and where these funds come from.

After discussing Objective 3, refer to TM: E1–2C to review the four main parts of a financial management plan.

Objective 4: Describe the different types of records kept in horticulture businesses.

Anticipated Problem: What are the different types of records kept in horticulture businesses?

- IV. There are two types of records kept in horticulture businesses, financial records and physical records. Both types are useful only if kept accurately. They are also important when reporting taxes to the government.

- A. Financial records include the balance sheet, income and expense summary, cash flow statement, and customer credit applications. Careful financial records can ensure a profitable business.
- B. Physical records include culture and production of horticulture crops, inventory records, machinery and equipment records, and labor records. Careful physical records can help a manager determine what the business has on hand, and when.

Explain to students that financial records are records related to finances or money. Physical records relate to the physical aspects of business including people and items. Use TM: E1–2D to review the definitions of each of these types of records.

Objective 5: Explain how to calculate the cost of products and services.

Anticipated Problem: How can the cost of products and services be calculated?

- V. Financial and physical records also have another use, calculating costs. Before a product can be marketed, its price must first be calculated. Businesses that offer services, such as landscape maintenance or floral design, must also set a price for their services.
 - A. The amount of money a customer pays for a product or service is known as the **selling price**. This is higher than the actual cost of the product or service. **Cost** refers to how much money the business actually spent on producing the product or service sold. There are two types of costs, fixed and variable.
 - 1. The expenses involved in running a business are called **fixed costs**. These costs are not directly related to the production of the product or service being sold. Examples of fixed costs are salaries and maintenance.
 - 2. **Variable costs** are costs directly related to the production of a product or service. These costs have a direct relationship to the amount produced, they are figured on a per unit basis. Examples of variable costs in a greenhouse would be seeds and planting media.
 - B. Service oriented businesses have to take special considerations when determining costs. The costs involved in providing a service include materials, labor, overhead costs, and profit.
 - 1. **Overhead costs** are the fixed costs of running a business.
 - 2. **Profit** is the money a business makes from a product or service after deducting the cost involved in producing it.

Refer to appropriate sections in the Introduction to Horticulture Activity Manual (also LS: E1–2A). Assign students to complete the worksheet at this time. TM: E1–2E can be used to review the different types of costs.

Review/Summary. Summarize the lesson by reviewing the student learning objectives. The anticipated problems can be used as student review questions. Chapter reviews from the books listed on the resource list may also be useful.

Application. The following student activity can be used to apply the student learning objectives: LS: E1–2A—Investigating Fixed and Variable Costs.

Evaluation. Evaluation should be based on student comprehension of the student learning objectives. This can be determined using the attached sample written test.

Answers to Sample Test:

Part One: Matching

1=f, 2=a, 3=d, 4=e, 5=c, 6=b

Part Two: Completion

1. fixed
2. variable
3. overhead
4. net worth
5. financial, physical

Part Three: Short Answer

1. compare past and present performance of the business, compare against other businesses in the same industry, compare against the company's objectives.
2. cash flow, profit and loss statement, balance sheet, list of sources and uses of funds

Test

Lesson E1–2: Financial Management in the Horticulture Business

Part One: Matching

Instructions. Match the term with the correct response. Write the letter of the term by the definition.

- | | |
|------------------|----------------|
| a. cost | d. liabilities |
| b. selling price | e. equity |
| c. profit | f. expense |

- _____ 1. the cost of producing a product
- _____ 2. how much money a business actually spent on the product or service
- _____ 3. debts of a business
- _____ 4. amount of money something is worth beyond what is owed on it
- _____ 5. the money a business makes from a product or service after deducting the cost involved with producing it
- _____ 6. the amount of money a customer pays for a product or service

Part Two: Completion

Instructions. Provide the word or words to complete the following statements.

- _____ costs are not directly related to the production of the product or service being sold.
- _____ costs are directly related to the production of a product or service being sold.
- _____ costs are the fixed costs of running a business.
- The difference between a company's assets and liabilities, their equity, is also called their _____.
- The two types of records businesses keep are _____ and _____.

MEASUREMENTS OF BUSINESS PERFORMANCE

- **Compare past and present performance of the same company**
- **Compare business performance against the performance of other businesses in the same industry**
- **Compare the performance of the business to the state objectives of the business**

BASIC FINANCIAL TERMINOLOGY

- **Liabilities—debts of a business**
- **Equities—amount something is worth beyond what is owed on it**
- **Capital—equity of the business owners**
- **Assets—elements on the balance sheet that show the resources of a business**
- **Revenue—increase in capital due to business transactions**

FOUR PARTS OF A FINANCIAL MANAGEMENT PLAN

- **Cash flow**
- **Profit and loss statement**
- **Balance sheet**
- **List of sources and uses of funds**

TWO TYPES OF BUSINESS RECORDS

- **Financial—balance sheet, income and expense summary, cash flow statement, customer credit applications**
- **Physical—culture and production records, inventory records, machinery and equipment records, labor records**

COSTS OF PRODUCTS AND SERVICES

- **Cost**—how much money a business actually spent to produce a product or service
- **Fixed costs**—expenses involved in running a business, not directly related to the production of the product and service
- **Variable costs**—costs directly related to the production of the product or service
- **Overhead costs**—fixed costs of running a business