



# MICRO-AID<sup>®</sup>

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## Conservation and Building of Equity in Livestock Production

### Introduction

Access and availability of capital have always been very important in agriculture including in the production of food and fiber from livestock. Recent cost increases in commodity feedstuffs and fuel have nearly doubled the cost of livestock production. There are several reasons for recent commodity increases that will remain in place over time such that this situation is not likely to change in the near future. With higher production costs, the competition for limited, available capital will become more intense. Therefore, the ability of producers to maximize their capacity to build equity when production is profitable and to conserve equity when production is not profitable is more important now than ever. This is especially important now while the industry and markets are adjusting to higher feed and production costs. Producers who can demonstrate a sound plan for equity conservation will ultimately have better access to available capital and will be much more likely to endure losses until profitability returns in the production of livestock to feed and clothe the world. Although the following examples are based on the production of pork, the same principles apply to other livestock and poultry production systems as well.

### How is Equity Defined?

Equity and debt are two types of capital. Capital provides the funding to own the assets required to run a business. Equity capital is the capital placed in the business by the owner(s) of the business. By intent, equity is the capital at the most risk and likewise has the most opportunity to generate a return. Debt capital is that which is borrowed from a lender or other entity at a pre-determined interest rate and normally paid back to the lender at an agreed upon schedule.

A simplistic definition of equity is the amount of money the owner(s) would have left after completely selling out the business and paying off all debts. Most businesses have a primary financial goal to increase owner equity 6%.

### How is Equity Generated?

Equity is generated from profit. Three examples, generated through the use of the Micro-Aid<sup>®</sup> Value Proposition Model for swine production, are used to demonstrate the flow of profits to the statement of financial position (often referred to as a balance sheet). All examples are for the same 2,600-sow farrow to finish operation. This operation owns all livestock and has production contracts for the facilities. Therefore, no facilities are owned or included in this statement. Additionally, income taxes have not been considered in these examples because the intent is strictly to demonstrate the flow of profit into equity.



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