

# AgriProfit\$

## Newsletter for Alberta Cattlemen

### Editor's Corner

After a lengthy hiatus brought on by, among other things, drought and BSE, we're "back in the saddle" with the *AgriProfit\$* Newsletter for Alberta Cattlemen.

The role of this newsletter is to bring you *timely information, analysis and applied research on the economics and business management of cow/calf operations* ... all focused on information and thought-provoking discussions on *what you can do to improve your cow herd's bottom line*.

**In this issue**, we're starting off a series on managing your cow/calf business through the aftermath of BSE. We'll be providing some information and insight for Alberta producers to mull over in charting the future of their businesses.

Diane McCann-Hiltz will bring us her views on the feeder calf market in the "Market Watch" section.

In the "So What ...?" column, Jeff Millang touches on the information and planning required to logically approach the task of managing through these times of uncertainty.

### Now What? - Managing Your Cow Herd in the Post-BSE Environment

Dale A. Kaliel

Sr. Economist: Production Economics

**S**o you survived the drought ... and were set to turn a tidy profit with this fall's calves. Then came May 20<sup>th</sup> ... arguably one of the darkest days in the history of Alberta's beef industry. I've been fielding questions from Alberta cow/calf producers on a regular basis that start out with ... "Now what do I do about ...?"

Invariably these questions focus on a specific decision. Do I keep my calves? Do I hold and re-breed my "culls". Do I sell my bred heifers into the slaughter market? The list goes on.

Now, more than ever, it's time to sit back and take a long hard look at the long term outlook for you and your farm as a participant in the Alberta beef industry, and particularly in the cow/calf business. I know the pressure is on to make a few decisions. But before you get to far down the road, take some time to *think strategically*.

#### Why Think "Strategically"

In my mind, there's an unsettling number of folks who are assuming that once the border opens, we'll go back to "business as usual". From my experience, and the information I've taken in, this assumption can be dangerous in a couple of

significant ways:

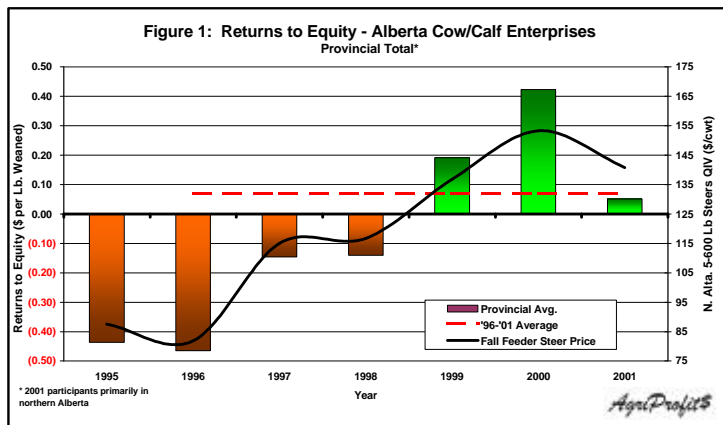
- < the "when" to a complete border opening could be weeks, months or years. In the meantime, partial trade constraints will create pricing "imbalances" that will filter back to calf and cull values in uncertain ways.
- < more importantly, the "if" of going back to "business as usual" looms large. My conclusion is that the industry will be faced with a new reality with pricing settling to a lower plane.

All-in-all, this will pressure businesses to re-structure. Changes at the margin, those incremental adjustments you've been making to improve your productivity and unit costing over time, will not be adequate in the "new industry".

How did I come to this conclusion? It comes back to "Why Do We Keep Cows?". If we're in the business for long run profit, then the historical economic performance of the cow/calf sector will tell us much about where we, as individual producers, need to go in the future.

#### It's In The Numbers

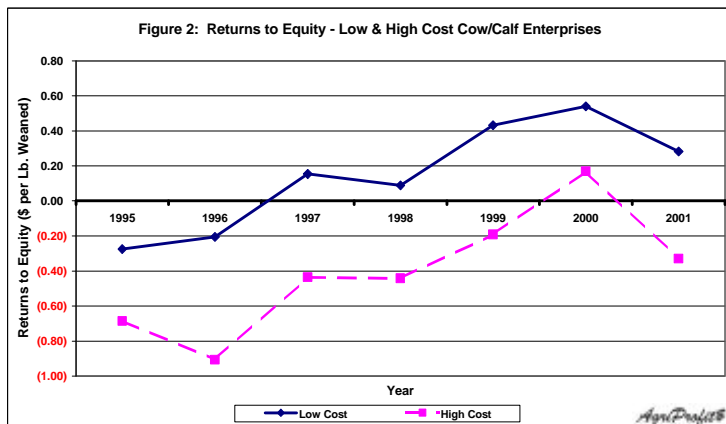
Let's take a look at an *AgriProfit\$* analyses for clues. The provincial *average* return to equity



(profit) for cow/calf enterprises over the seven year span of 1995 - 2001 is shown in Figure 1. The six year average profit for the '96 to '01 period was \$0.07/lb. weaned. It's important to recognize, when looking at these averages, that:

- < many of these *AgriProfit\$* herds are part of multiple-enterprise farms. Often the "other" enterprises cash flow the cow herd through the leaner times. Over the longer term, however, the cow herd needs to turn some level of profit.
- < Alberta is a large and diverse province. Averaging over the province masks annual and regional events that push this average either way. Individual performance over this time may vary significantly from the average.
- < as averages they imply that there are producers above and below this mark.

Events like BSE will depress market prices and, as a result, pressure profits down over the long haul.



On to the next step. You have little control over market prices, and ultimate control over your unit production costs. I've shown the profitability of high and low cost *AgriProfit\$* herds, as separate groups over time, in Figure 2. Low cost herds are consistently profitable and, more importantly, contribute to overall net farm income and risk reduction. Conversely, high cost herds rarely pay for farm resources utilized, are a net drain on farm cash position, and put the rest of the farm at greater financial risk.

## Strategies ... and More Strategies

The post-BSE world will likely mean market prices will settle at a new, lower level. Considering the historical costing relationships, there is simply too much at stake for producers to avoid being long term and strategic in their management.

But how does this translate into a "business strategy" for cow/calf producers? Brester and Penn<sup>1</sup> laid out the notion that businesses have the choice between "differentiated" and "low cost" strategies to remain competitive. The "differentiated"

strategy implies you invest in producing something sufficiently different from your competitors that the market will pay a premium for. To follow this strategy, you've always got to be a step ahead in being "different". There are added costs and risks.

Following the "low cost" strategy implies that you invest in structuring your business to aggressively capture cost efficiencies. A portion of profits are re-invested in continually grinding down unit costs to improve margins.

You'll want to set your strategy as to how you will respond. The low cost approach is likely the strategy of choice for most Alberta producers. Jeff Millang will present a twist to this discussion on business strategies in the next *AgriProfit\$* newsletter.

## Home Stretch

We'll need to take a hard look at our production systems, gearing up to make some fundamental changes in facilities, equipment and land we will deploy over the long term. The aim will be leaner production systems, combining feeding and grazing resources with a different approach to how and with whom we do business.

Dale A. Kalliel

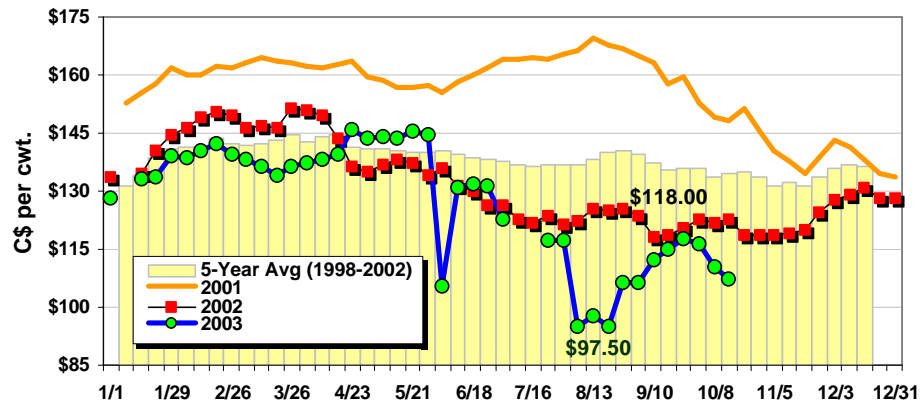
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1. Brester, G.W. and J.B. Penn, "Strategic Business Management Principles for the Agricultural Production Sector in a Changing Global Food System", Trade Research Center, Montana State University, Policy Issues Paper No. 11, Nov. 1999

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## Market Watch

### Northern Alberta 5-600 lb. Feeders Weekly Average Steer Price



Source: Carfax; Economics & Competitiveness Division, AAFRD

Near the end of September, Alberta calf prices were approaching price levels of last year. However, since then prices have decreased significantly from \$117.53/cwt to \$107.14/cwt. Typically, calf sale volumes will pick up momentum during the last three weeks of October. If calf prices continue to fall, many cattle producers will retain ownership of their calves in an attempt to wait out the price weakness.

Before producers decide to sell calves now or retain ownership, they need to consider:

(1) individual cash flow needs; (2) risk-taking position (financial position); (3) available facilities and feed and water resources; (4) available time; and (5) experience in feeding calves. Producers need to carefully weigh their financial and physical positions to make the decision for this year's calf crop. By assessing the above points, calculating their cost of production and potential return, not only is the decision-making process less stressful but there is a better chance the decision will be the "right" one.

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We'd like your comments and questions about the articles featured in this newsletter. Suggestions for future issues are also welcome. Please contact me at:

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If you'd like to learn more about and/or participate in our research program, please contact me at the above.



If you're interested in the CowProfit\$ software, training or seminars, contact:  
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# So What's .. So Hard About Managing?

Risk has certainly been the name of the game for the Canadian beef industry and will likely remain as an industry feature some time to come. I've had many discussions with producers, industry experts and government staff, and one thing for sure is *we have a whole range of futures that could happen*. If we throw in the element of time, the scenarios and choices get even larger ... ***Managing is hard***.

Why do we care about the future? Well, we are trying to evaluate and make choices in an uncertain environment. With the margins in beef production getting tighter and tighter every year, one wrong decision can have disastrous effects.

***Managing is hard*** ... with so many choices how do you decide? First and foremost, there is only one decision that matters to you and your business ... that is your decision. What your neighbors decide to do is their decision and reflects their knowledge and beliefs about what prices may or may not do, or whether the border will open in 60 days or 600 days.

What you can do is seek as much varied and informed opinion as possible. While the coffee shop may be a great place to gather information, there are certainly other sources. In the BSE world, talk with the industry organizations. You can utilize the CCA's BSE information website and phonenumber. Talk with your organization delegates and see what they know. Talk with industry experts, or read what they have to say in their information newsletters or interviews.

The next step is to take this information, evaluate the credibility and likelihood that the sources are informed and knowledgeable, and apply what you know. From this base you can form a couple of scenarios that are likely going to unfold. Then you can define plans for these things happening, and what you are going to do when, not if, they happen.

Talk to the stakeholders in your business about the scenarios you've put together, and about the implications they may have for them. Your business stakeholders may include lenders, family, and input suppliers. ***Preparation is a challenging part of managing your business***.

Once you've worked through your scenarios and impacts with your stakeholders, you can move on to the next critical step. Remember, risk is a double-edged sword. We typically focus on the negatives or down-side of risk, but it may also bring business opportunities. Building on your scenarios and plans, define actions to reduce the bad impacts or take advantage of the opportunities.

Although this may seem a simplistic approach, during uncertain times, ***managing is hard*** ... breaking down your information gathering, analysis and decision making process into smaller, defined pieces can often make the task seem clearer and less daunting.

Back to the cow calf world, common decisions producers are facing include, "should I ... :  
< keep my calves all winter? ... maybe  
< sell my bred heifers into the feedlot, hoping they grade under 30 months of age? ... maybe  
< sell some, or all, my cull cows for \$0.20/lb. or keep them all winter to rebreed some, or all, of them? ... maybe

How do you know? We expect the cow calf sector to be cash poor this fall. Take stock of your financial position. Cash flow management will be key to riding this incident out and positioning your business for the future. ***These all depend on what you have determined to be the most likely scenario for the future***.

Our perception of the beef industry has changed, and likely our position in the global marketplace has changed, too. We have new aspects to our production chain, and new challenges to specific products and classes of animals. At the same time there is opportunity to expand and grow our industry. Investing time in managing your business will be the key. A few timely quotes come to mind, ... "may you live in interesting times", and ... "it was the best of times and it was the worst of times."

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