BeefTalk: High-return Operations Are Becoming High-cost Operations

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Rain is good, but the timing and quantity certainly are a point of discussion. The cattle business, a business that essentially is birthed from the grass business, certainly has more flexibility to roll with the wet times than other agricultural enterprises. However, even the cows are beginning to look for a dry knoll to bed down on.

During a spring of excessive rain, the lack of heat has held back grass production. The discussion of grass is core to profitability. Generally, the lack of grass means there will be a reduction in stocking rates and ultimately a reduction in herd size.

In fact, producers generally are engaged in the perpetual balancing act between expenses and income. As producers struggle, the scale tips quickly to the negative when feed resources are jeopardized.

In reviewing the North Dakota Farm Management education program (http://www.ndfarmmanagement.com), along with FINBIN (http://www.finbin.umn.edu/) data from the Center for Farm Financial Management at the University of Minnesota, the balancing act between expenses and incomes becomes very real.

An overriding business principle is the basic concept of gross margins. As a producer, when a producer understands gross margin, he or she can start to appreciate what dollars are available to work with.

According to Jerry Tuhy, Bismarck State College farm business management instructor at the Dickinson Research Extension Center, gross margin accounts for the purchase and sale of all calves, cull cows and bulls, plus animals transferred in and any overall changes in cattle inventory.

In the big picture, if gross margins are very small, there isn't any money to work with. If gross margins are high, the opposite is true and producers have money to manage and allocate funds to various phases of the beef enterprise.

Let's return to previous discussions regarding gross margins for those producers who have at least 50 cows and are involved in the North Dakota Farm Management education program. Particularly, let's look at 2010 and the combined years of 2004 and 2005. These years are used because they had the greatest gross margins available to beef producers in recent times.

The gross margin for 2010 was $578. For the combined 2004 and 2005 years, the gross margin was $596. The difference between the two periods is real. In 2004 and 2005, the average producer captured a little more than 34 percent of the gross margin as net return. In 2010, the average producer only captured a little more than 19 percent as net return.

This is a huge difference and should be pondered by all producers. One conclusion that seems to repeat itself is that times have changed. Even with available money, producers need to realize that the opportunities of creating more wealth are not as easy.

In 2010, even though average gross margins were significant, producers who were in the upper 40 percent based on net return had a gross margin of $614. These producers had a positive $188 net return per cow and captured a little more than 30 percent of the available gross margin as net return.

The top producers did better than the average of all producers. However, they apparently were not able to change their cost structure to the extent that producers in 2004 and 2005 could, they simply were dealing with more money.

If we go back to 2004 and 2005 to see if the same pattern was evident, we again looked at the upper 40 percent of the producers based on net return. These producers had a gross margin of $645, which was higher than the 2010 high-return producers. These producers managed to capture more than 45 percent of their gross margins.

A striking thought is that those producers who are in the upper 40 percent of net return were there apparently by increasing gross margins with limited capacity to control costs. Meanwhile, if we go back a few years when gross margins were high as well, the high-net-return producers increased gross margins and also had a better handle on costs.

Therefore, these producers captured 45 percent of their gross margins versus only 30 percent of current producers. A complicated fact is that it is no longer easy to simply manage an average or above-average cattle operation based on net returns when gross margins are high.

So, the question of how a producer sustains a cow-calf enterprise remains.

May you find all your ear tags.