Beeftalk 759: Can Profitable Beef Operations Go Broke?

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Even though the weather is mild and the feeling of spring is here, remnant thoughts of winter still are fresh.

One thought that we should be pondering is business records. Every farm and ranch should have completed their yearly records or be in the process of completing them.

There is the question: Can profitable beef operations go broke? Absolutely, is the answer. Why? For one thing, the definition of profit is misused. And the longer the wrong numbers are applied to the word “profit,” the more likely an operation can get into financial trouble.

Ranch and farm records, unfortunately, are very diverse, which results in difficulty in clearly understanding what the records mean. Care needs to be taken to make sure the numbers used are the numbers needed to answer the question. The market price of a calf minus the direct expenses of producing that calf often is stated as profit. However, that calculation is far from any indication of the financial status of a beef operation.

This very narrow and selective approach to business discussions makes good coffee shop talk but may or may not pay for the coffee. Starting with tax preparation, loan renewals, checking account balances, gross margins, direct and indirect expenses, depreciation, net returns, labor and management charges, and, ultimately, return on total assets, the mind can go numb.

Even further complicating the process, not all professionals use the same business evaluation process, so there are more questions.

Keep in mind, the producer is the endpoint of this discussion. The various enterprises utilized within a producer’s business may calculate a profit-and-loss scenario in their own right. These “profit centers” are not the endpoint of the financial analysis.

Another interesting point is that even the source of funds is a “profit center” for a financial institution but is a cost to the beef operation. “The bank is happy” saying may not correlate well with a producer’s expectations. Collateral will leverage a smile out of most bankers.

Again, if beef producers really want to understand where their beef operation is financially, the appropriate analysis must be done. The right process is much like during the ’90s’ when integrated resource management programing efforts were being offered by many universities involved with beef cattle and the National Cattlemen’s Beef Association.

At that time, a standardized performance analysis (SPA) program was developed for in-depth evaluation of cattle operations. The purpose of the program was to assist producers in evaluating and reducing their cost of production while improving their production and marketing efficiency. The process was completed and is available today athttp://www.beefusa.org/spacalculationsworksheet.aspx.

The real answer to the question of profit rests with the ability to complete the SPA process or a process that fundamentally provides the same information through a business evaluation. Why is this important? The dynamics of the beef business change, and yet the beef producer is trying to focus down the road.

Sometimes, the question is retirement or family expansion. Sometimes, the question is trying to cover increasing overhead costs or the producer simply wants to change his or her lifestyle. All these are difficult questions, and no one wants to initiate a reorganization of the business without the right data in front of him or her.

Bringing new partners or family members into a business organization, plus funding the retirement of the previous generation, would be disastrous if the operation is not financially viable.

What if the value of the assets of the beef operation would return more dollars invested in a different financial portfolio? Who ultimately pays for multigenerational demands on the fiscal resources of the operation? These are not words of comfort, but they become words of pain if not asked before a reorganizational plan is implemented.

The point is that the current generation needs to provide the financial analysis that will determine an acceptable return on total assets (ROA). Knowing the actual current ROA is needed to establish a future goal. If the ROA is adequate, life is good. If not, than evaluate and reduce the cost of production and improve production and marketing efficiency. Then start planning for the next generation.

Standardize Performance Analysis

The Goal: Set an acceptable return on total assets

The Action: Evaluate and reduce cost of production while improving production and marketing efficiency

The process of fiscal evaluation of a beef operation never will be simple. However, remember the initial question: Can profitable beef operations go broke? Absolutely, so do your homework.

May you find all your ear tags.

Your comments are always welcome at http://www.BeefTalk.com.

For more information, contact the NDBCIA Office, 1041 State Ave., Dickinson, ND 58601, or go to http://www.CHAPS2000.com on the Internet.