

## Budgeting and Farm Systems Under a Lower Payout

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Over the last four years only farm expenses on NZ dairy farms have gone from \$3.20/kgMS, up to \$4.60/kgMS and then down to approximately \$4.20/kgMS last year<sup>1</sup>. With a decline in payout from \$7.60/kgMS in 2007/08 to \$5.20 last year and a forecasted \$4.55/kg this year, it is obvious that cash flows will come under pressure and high cost structures will need to be revised downwards.

For most, it will be necessary to get cost structures down below \$3.40/kgMS just to break even.

The Southland Demonstration Farm is in a unique position to show leadership in this area and show that it can be done. The farm has been through many ups and downs that are commonly seen in the farming community – labour and management issues, lower than desired production, and high cost structures. It is also very much a commercial farm. Its equivalent debt levels are no different than that of the general dairy community. It has to front up to the banks just as every other farmer.

No one would argue that achieving a \$3.40/kgMS cost structure is an easy task. It is hard and many difficult decisions need to be made. To achieve this, every expenditure heading needs to come under review. Farmers will need to make decisions as to what expenditure is non negotiable, what is negotiable, and what is necessary to achieve the goal. It will be necessary to assess value for money and this differs at a high payout vrs a low payout – we can justify anything at a high payout.

There will be pressure from goods and service providers to ensure that their cost is the last to be cut. Everybody thinks that their product or service is the most important expenditure item on your farm. Farmers will have to be quite dispassionate and objective. Some products and services have long term value but less short term value – do we farm for today or do we farm for tomorrow?

Over the last six years, I have annually analysed the feed management systems of my clients<sup>2</sup>. Much of the theory and analysis of this is similar to that shown in the DairyBase Physical section. The analysis shows interesting trends and identifies areas of strengths and weaknesses for clients so that they can target improvements for the future.

- 2005/06 2006/07 2007/08 2008/09

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<sup>1</sup> DairyBase and includes wages of management and other non cash adjustments

<sup>2</sup> Agribusiness Annual Feed Review

SR at Peak	2.79	2.80	2.90	2.86
KG LW/tDM	91.0	90.5	99.0	91.4
KgMS/ha	1138	1176	1171	1180
Cow wastage	16.4%	13.3%	11.8%	13.6%
Bought in feed/kgMS	2.18	2.4	3.2	2.5
Utilised Pasture t/ha	11.1	11.5	10.4	11.55
Margin/ha	\$4255	\$4760	\$8040	\$5298
Margin/ha @ \$4.10	\$4255	\$4337	\$3901	\$3975

Over time we have seen a general lift in stocking rates, production and utilized pasture. This reflects improved management and the establishment of farms post conversion.

A couple of concerning though are that our bought in feed has lifted from 2.18kgDM/kgMS to 2.5kgDM/kgMS and that cow wastage is still too high.

Bought in feed includes nitrogen application but this is not the reason and average application has actually fallen. The increase in bought in feed (15%) is thus either bought in silage or concentrates.

In my analysis I try to put an economic analysis on it by valuing all feed inputs and cow wastage to calculate a net margin. From the above you can see that the margin has lifted with payout but when you adjust it back to a \$4.10/kgMS payout our margin has actually fallen. This raises questions about how economic our productivity increases are. 2007/08 figures are affected by last years drought.

My analysis is similar to that carried out by DairyNZ<sup>3</sup> on behalf of SIDDC and shows very similar correlations between pasture production and profitability even though their analysis was more details and used full DairyBase Analysis<sup>4</sup>.

This year I have further analysed the difference between those farmers who are basically all grass farmers vrs those whose feed significant amounts of concentrates (45% of database):

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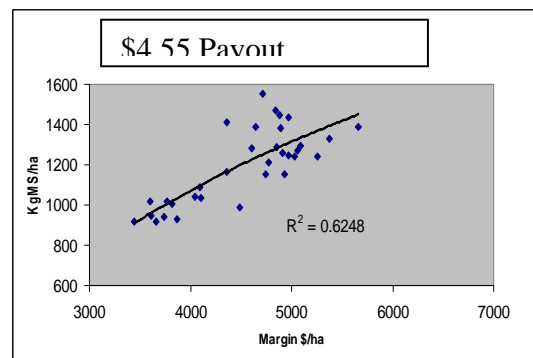
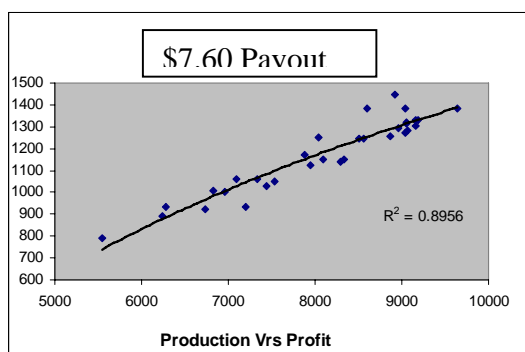
<sup>3</sup> DairyNZ presentation to LUDF Focus Day 2<sup>nd</sup> July 2009

<sup>4</sup> DairyBase is the NZ dairy industry financial and physical database.

	<u>All Grass</u>	<u>Concentrates</u>
SR at Peak	2.82	2.95
KG MS/KGLW	0.83	0.88
KG LW/tDM	89.9	93.3
KgMS/ha	1129	1266
Empties	9.3%	8.4%
Concentrates Fed (kg/head)	34	467
Bought in feed/kgMS	2.02	3.17
Utilised Pasture t/ha	11.6	11.7
Margin/ha	\$5264	\$5372
Margin/ha @ \$4.55/kgMS	\$4540	\$4585

From the above you can see that concentrate feeders have a higher stocking rate (5%) and produce more milk (12%). Their cows are more efficient at converting liveweight into milk (presumably because they are better fed) and they have a lower empty rate. Pasture utilization though is similar and the conversion ration for the extra feed input is a very poor 9.4kgDM/kgMS.

At a \$5.20/kgMS payout the concentrate feeders were earning approximately \$108/ha more. At a \$4.55/kgMS payout the net return though would have only been \$45/ha.



The relationship between gross margin and production gets more blurred the lower the payout is. That is, with a high payout feed inputs are easily justified ( $R^2 = 0.89$  at \$7.60/kg) but not so at a low payout ( $R^2 = 0.62$  at \$4.55/kg). It's a pretty simple message but almost half of high concentrate farmers did not make anymore net income than their all grass counterparts last year.

This is not saying that concentrate feeding is not economic but optimizing pasture utilization has to remain the number one priority at all payouts.

