Economics & Competitiveness

AgriProfit$

Newsletter for Alberta Cattlemen

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Editor's Corner

We're coming down the home stretch, where you're about to get paid for your years' time, effort and investment in getting those calves to weaning. Up to this point, you've worked on the cost side of the equation. What's left is pulling the trigger on your marketing plan, and realizing on your hard work.

In this issue, Chris Panter, Alberta Agriculture's Livestock Market Analyst, has served up a review of beef market fundamentals and outlook. He's walked through a series of local, North American and global events that have shaped the prices we see today and go on to leverage the drivers of intermediate and long term price trends and price volatility.

Chris has documented the key features in this fall's market, how it translates to potential prices, and how this turns into strategies to market your '13 calf crop.

In the "Coming Events" section, Abby Verstraete fills us in on the upcoming Cow/Calf-enomics Workshops. I've also posted a web-link to see events brought to you by your local forage and applied research associations.

In the **"So What …?"** column, I've posed the question "So What's Your Return on Investment?" … do you know what you're earning on your investment in your herd and your operation? ROI can be a valuable performance measure in the business. I've laid out how you can calculate it and use in making effective business choices.

Dale A. Kaliel, Editor

Market Fundamentals and Outlook

Chris Panter

There just doesn't seem to be a lot of downside risk in the calf market this fall … an observation that you've likely heard from a number of sources recently. There's a number of factors that have played out over this past year, bringing us to this point.

Knowledge of these factors and how they will affect your pricing is key in defining how and when you put your calves out to market. What strategies for marketing calves and cull cows can maximize returns at a reasonable risk?

High prices can distort risk perception, and sticking to "the plan" is just as important when the market is up as when it's down. A period of strong prices can be an opportunity to solidify your profit and position the farm for the future.

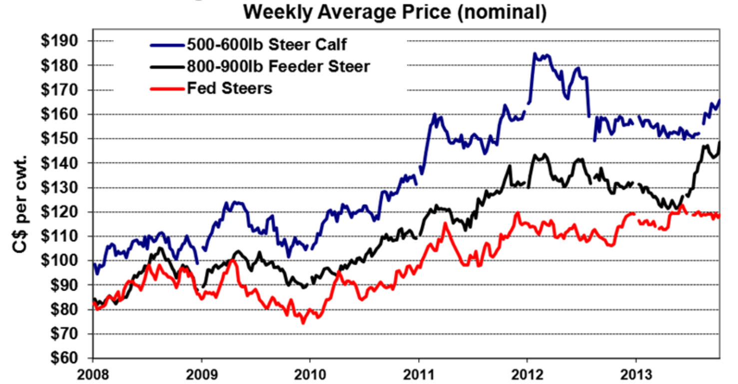
Market Prices

Cattle prices in Alberta were generally rising from 2008 to 2012. Feeder cattle prices declined from early 2012 until the middle of 2013. Fed cattle prices remain strong on robust beef demand and a limited supply available in North America due to a smaller cow herd.

Feeder prices are more volatile compared to the price of fed cattle. Greater volatility means more risk to your take-home price.

The market for 800-900lb yearling steers increased considerably this year (Figure 1), from $121/cwt. in May to $147/cwt. in August. Prospects for lower feed grain prices were partly responsible for the 21 percent rise.

Figure 1. Alberta Cattle Markets
Weekly Average Price (nominal)



Source: Canfax; Economics & Competitiveness Division, AARD

Last years' drought in the US and eastern Canada drove corn and barley prices up to the point where feedlot margins were squeezed with little chance of profit. There are signs this situation is beginning to change.

Calf prices are driven primarily by feed costs and the price of fed cattle on the futures market. Calf prices are also impacted by the exchange rate.

Canfax estimates a 1 cent drop in the value of the Canadian dollar relative to the US dollar, adds about 3 cents per pound to the price of calves. The Canadian dollar weakened and the futures board posted strong settlement prices in recent months.

All-in-all, there is some movement in elements that affect the near and intermediate term calf prices. It's worth doing some research into when you think these will start to turn, and then, how you might adjust your herd operations and marketing strategies to compensate.

Labeling and Trade

Wide spreads between calf prices in Alberta compared to the US increases pressure to ship calves south. Canadian feeder cattle exports are running higher in 2013 (January-August) compared to the past three years. Feeder calf prices are strong, trading above $160 per hundredweight in October.

Enhanced MCOOL rules set for full implementation in November, could impact the demand for Canadian feeder cattle in the US market negatively. The US Government shutdown and debt ceiling debate also injects uncertainty into the market.

The "fall-run" could test prices as a greater volume of lighter weight animals hit the market from mid-October to early-December. Well documented excess capacity in the feedlot sector combined with producers holding back heifers might support calf prices.

Knowing this, the question producers are posing is, "what is a sensible approach for a cow/calf producer marketing feeder calves in 2013?" I'll start by saying last year taught us a lot.

Fickle Calves

The price of 500-600lb steer calves were at record highs in the first half of 2012. Fallout from the US drought depressed calf prices by about $30/cwt. in the brief period between June and August.

Next came the XL Foods beef recall and record high feed grain costs, calf prices remained subdued until August of this year.

What the market tells us and what it ends up doing can be two different things. For example, last year the market signaled high feed costs, depressing prices on lighter calves and giving incentive to background them on forage. The market was paying better for heavier weight classes that feedlots could turn around faster.

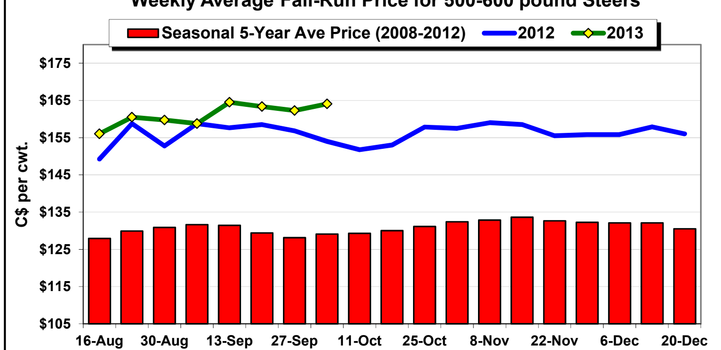
Earlier this year, as many of last years' retained feeders approached the 800 pound mark, prices for that weight class softened and profits disappeared. This fall, the interplay of similar price drivers will affect retention and feeding choices.

So, if your business model as a cow/calf producer is to wean and market calves at a certain weight, say 500-600 pounds, there's some key notions to consider before committing precious feeds and operating expenses to retaining and backgrounding calves. Ask yourself:

- What's my target weight?
- Can I feed to get that gain?
- What's my (total) cost of gain to get there?
- What do I expect the price to be at that time?

Looking at the pricing patterns in Figure 2, while we don't expect much of a downside, the real question is, "what's in the market that suggests it will move up significantly?" If the market's flat, profits are pinned to beating cost of gain and the price slide. Without a good handle on the cost of backgrounding and the related market risks, a cow/calf producer may be feeding cattle for free.

Figure 2. Alberta Feeder Cattle
Weekly Average Fall-Run Price for 500-600 pound Steers



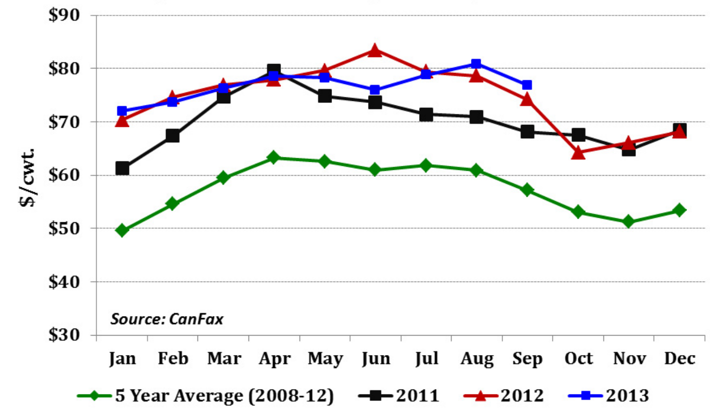
Source: Canfax; Economics & Competitiveness Division, AARD

Strategic Heifer Retention?

There seems to be some reasonable strength in the intermediate and long term cattle markets. This begs the questions, "Is my herd young enough?", and "should I be expanding my herd?" Run your pencil through a few retained heifer and bred heifer budget scenarios.

Average bred heifer prices traded above $1,200/head for quality stock earlier this year. Retaining heifers can be a cost effective way to expand the herd. They also give you the flexibility of being readily marketable at any point in time. You've got a good year before you have to commit to a final choice. Whether you keep them or sell them, there can be a profit opportunity.

Figure 3. Alberta Average Monthly D1-D2 Cow Price



Robust Ground Beef Demand

Cull cow prices remain solid. When we're running a good $20/cwt over the long term average price, it's hard to make the case for keeping underperforming cows.

In 2013, D1-D2 cow prices tracked last year's seasonal moves quite well. The August and September monthly average prices were higher than '12 and about 35 percent above the five year average. Given the high demand for grinding beef, cull cow prices should remain above average for the rest of the year.

While prices are averaging higher than previous years (Figure 3), the usual pattern of seasonal decline for cull cows is still anticipated going into November. Feeding cull cows past this period begs the same questions as did the feeder calves.

What's your strategy?

Human nature and price-risk perceptions are not a business manager's friend. Optimism and a focus on the "high side" can cloud price projections. The manager's job requires a cold hard assessment of the range of expected prices along with potential upswings and downswings.

If you feel your herd is, on average, long term profitable, then you'll know that there will be periods of low prices that will eat away at this long term average … and periods of strong prices that shore this average up. Your marketing strategy should have you being "defensive" at the right time, cutting out the bottoms, and "offensive" at the right time, riding the upswings. Both of these demand that you get a sense for the risks, and "release" when the odds are realistically switching against you.

Your marketing plan should include price, revenue and profit targets based on realistic price expectations. Once you've hit these targets, if there's no tangible, realistic upside left, pull the trigger and realize your profit. These good times are when you finance the changes that make your business better in the future.

Home Stretch

The way local feeder cattle pricing is shaping up, it's important to pay attention to market signals (trends and volatility), and know your cost structure, for your herd and for fed cattle. Plan out your marketing and manage risk.

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Mark Your Calendars! … Cow/Calf-enomics: 2013 is Coming!

Tools and Strategies for Better Decisions: Risk Management & Profitability in the Alberta Cow-Calf Sector

Cow/Calf-enomics workshops are designed as information and discussion forums for Alberta producers. They address a broad range of timely and topical issues and opportunities that producers have in front of them … all in pursuit of long term profitability and dealing with risk.

Building on last years' success, Alberta Agriculture and Rural Development (ARD), along with industry partners, are continuing this seminar series at 4 locales across the Province this fall.

On the agenda…

This year's seminar theme is "Tools and Strategies for Better Decisions-Risk Management and Profitability in the Alberta Cow-Calf Sector". Topics include:

- Risk and Opportunity and Today's Markets – Anne Wasko/Debbie McMillin
- Introduction to Futures, Options and Cattle Price Insurance - AFSC/ARD
- Measuring and Managing Calf Price Risk - ARD
- Handing over the Reins-Transition the Ranch-Barrie Broughton QC, TEP
- Accessing Capital-Yours and the Banks - ARD
- The Future of Alberta's Beef Sector: A Young Producer's experience in getting established in the Beef Business - Local Producer

This year's sponsors …

Cow/Calf-enomics is the fruit of the efforts of a number of organizations serving Alberta producers. This year, Alberta Agriculture and Rural Development has partnered with Agriculture Financial Services Corporation, Farm Credit Canada, Alberta Beef Producers and Agricultural Research and Extension Council of Alberta.

Where and when are the seminars?

- Nov. 25th: Vermilion Regional Center
- Nov. 26th: Veteran Community Hall
- Nov. 27th: Olds College, Student Alumni Center
- Nov. 28th: Lethbridge-Country Kitchen Catering

How do I register?

The Ag Info Centre is handling Cow/Calf-enomics registrations this year. To book your spot, please call the Center at 1-800-387-6030. The registration fee of $25.00 includes lunch. Alberta Beef Producers are covering student admissions this year, *but students must register in advance to take advantage of this offer.*

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Coming Events:
A wide range of producer workshops & seminars are available through local forage & applied research associations. Visit the ARECA website at:
www.areca.ab.ca/events/upcoming-events
to see what's coming to your locale!

Would you like to receive the "***AgriProfit$*** Newsletter for Alberta Cattlemen" directly by e-mail?
Just drop me an e-mail to:
dale.kaliel@gov.ab.ca
and I'll put you on our e-mail list!

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

by e-mail: dale.kaliel@gov.ab.ca   by phone: (780) 427-5390
or, by mail: #302, 7000-113 Street, Edmonton, Alberta T6H 5T6

AgriProfit$

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

Manage Your Business Using Information About Your Farm!

Doesn't it strike you as odd that folks can tell you what you *should* do without knowing:

- what it costs you to do what you do, let alone …
- what it will cost you to do what they say?

Me too … I'm pretty sure your costs and their costs are different. Your seeding rate, fertilizer application, tillage practices, feed supplement, etc. are different … it's what you do on your farm. If you're managing your business for profit, shouldn't your budgets use your costs and yields?

AgriProfit$ delivers your farm's cost info

Alberta Agriculture's ***AgriProfit$*** team is preparing for the next program season. We're enrolling producers, and organizing the on-farm interviews to collect information that turns into business analysis reports for each participant. If you want cost of production information to manage your business, you can get it through ***AgriProfit$.*** If you're new to ***AgriProfit$,*** you'll be asking, "what's in it for me?"

What's in it for producers?

Participation in the ***AgriProfit$*** program is free-of-charge. It requires an investment in time from producers and we try to deliver value to ***AgriProfit$*** participants in return. Each receive:

- a detailed enterprise economic analysis, driving at unit costs and returns for their commodities,
- a "whole farm" analysis, revealing financial performance, strengths and weaknesses,
- benchmark analysis, laying out their own productive, economic and financial progress over time, as well as comparisons to "peers".
- newsletters, bulletins and analysis tools, based on standardized ***AgriProfit$*** information.

Participants are in the position to measure costs, performance, and take active management control.

How can *AgriProfit$* help producers?

The link between ***AgriProfit$*** and farm business success can be summed up in two phrases:

"You Can't Manage What You Don't Measure"

To reduce unit costs and improve profitability, the first logical step is to measure your "current position". A basic business analysis, including key enterprises and a roll-up to the farm financial position, is a starting point. Your analysis and budgets are *based on your farm.*

"Who's in Control of this Business, Anyhow?"

Without a business analysis, a farm basically directs itself. Knowledge of unit costs and financial performance helps producers focus on making the right choices …

… doing things right, ie. being cost effective, and

… doing the right things, ie. choosing the most profitable alternative.

Your analysis helps you measure success - how each choice improves farm profits, with acceptable risks. The manager is now in control.

How is my information used?

The confidentiality of individual producer information is paramount. In addition to business analyses for participants, pooled producer information is used in benchmarking, applied analysis, and decision tool support. The focus is on creating "knowledge nuggets" and decision aids based on real farm information.

Doesn't my accountant do this?

Although you may get similar farm level information from your accountant, it:

- often masks things you could do to manage for profit within your operation.
- doesn't deliver unit costs of production.
- is not typically comparable to broad-based industry economic benchmarks and analysis.

These differences may seem small but can make a big difference in how effective you can be in using your own "on-farm facts".

Does *AgriProfit$* have local partners?

AgriProfit$ staff work closely with local forage and applied research associations, adding value to local trials and demos, and bringing the economics and business management messages home.

Home Stretch

An ***AgriProfit$*** business analysis is designed to *measure* so producers can *manage*. If you would like to sign up to ***AgriProfit$***, or have questions, don't hesitate to contact me by phone (toll-free using the 310-0000 line), or by e-mail.

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So What's ... Your "Return on Investment"?

Return on investment (ROI) is a common term relating an business' rate of return on the inputs, both cash and non-cash, that were invested. It can be a valuable performance measure for monitoring and managing your business.

How's it calculated? … What's it mean?

ROI is, simply, annual profit as a percent of total investment. At the commodity level, this is revenues less production costs all divided by the investment it takes to produce it (breeding stock, equipment, facilities & land). Return on Assets (ROA) is the sum of all the farm's activity.

Evaluating a farm choice (an investment) involves considering both how much return (profit) *and* how it varies from period to period (risk).

How can ROI's & ROA's be used?

Rates of return can be used to compare different parts of your farm, different production activities, year-to-year progress, or your farm to benchmarks. They can be used for historical evaluations as well as targets for the future. The attached benchmarks give context to common uses for "ROI" including:

How do your commodities compare?

Stacking up ROI's on specific crops or livestock production activities gives insight into potential differences in profitability and risk. The "low cost" beef herds appear to have steady, positive ROI's. Returns on forages and grazing show steady earnings with less downside.

How do your crop plans compare?

Crop plans are a mix of different crops, rooted in agronomic realities. Step past individual crops to assess ROI's of crop mixes or rotations you use … some of which will be combinations of lower valued crops and higher valued crops. ROI's of the combinations will be averages of their components. Will risks be additive, too?

Are your enterprises pulling their weight?

Comparing ROI's between enterprises is an effective way of identifying areas of business strengths and weaknesses. Do enterprises complement each other (eg. cow herd and pasture) have positive, similar ROI's? Should they? When together do they add to ROI and reduce risk?

How about my farm's ROA?

If you're making good choices at the enterprise level, you should be getting maximum farm ROA. Ask the question, "which commodity or enterprise is a drag on profit or increases risk?" Looking at the charts, one interpretation is that the cow herd, forage and grazing enterprises complement each other, adding to returns and reducing farm risk.

Home Stretch

The charts below show average rates of return in selected ***AgriProfit$*** profiles over 17 years … how do you stack up? Why? If you'd like to generate these measures for your business, give us a call and we'll sign you up on ***AgriProfit$*** today!

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