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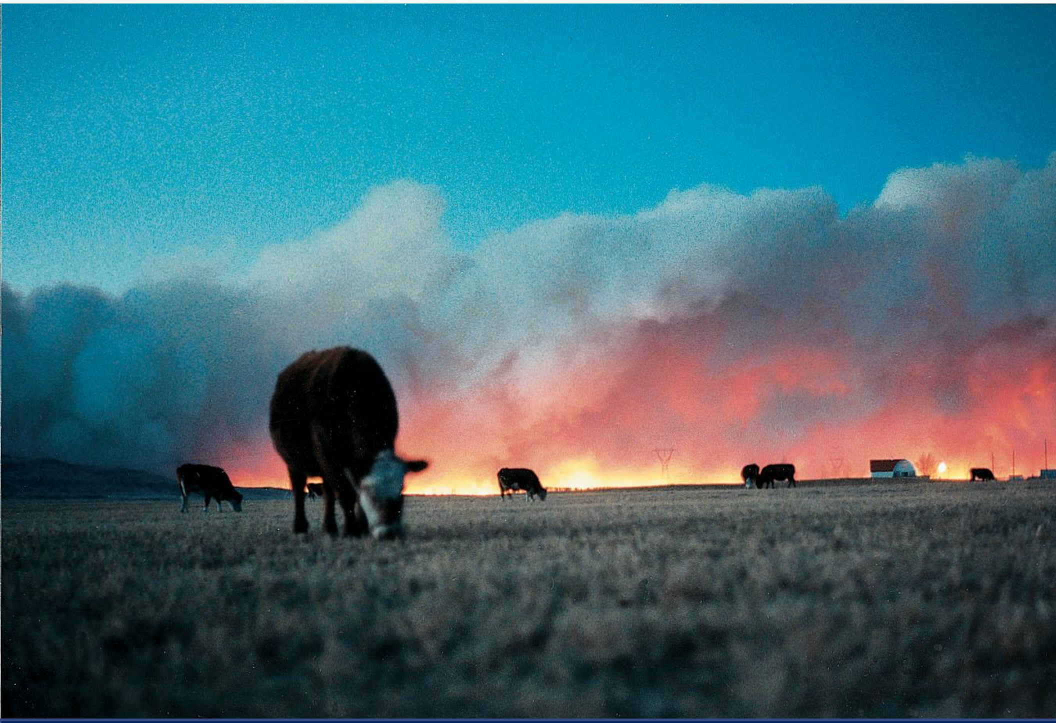

How to Blow the Family Farm – In 11 Easy Steps!

A satirical look at the common mistakes made in the family farming business

By Ryan Copithorne of Cows in Control Inc.

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Overview

How to Blow the Family Farm in 11 Steps is meant to be a lighthearted look at the pitfalls that many family operations experience. Having been part of a family farm operation and having spent years watching the cattle industry struggle with failed or failing family farms, I felt compelled to offer this quick-read document as a way to bring attention to my observations of what are the anchor chains holding back success for many family farms. I hope that it will be constructive in coming up with viable solutions to make family farms survive and thrive in years to come.

My background is mostly in the beef sector, but most of the concepts apply to farms and other agriculture businesses universally.

There are four types of people most farmers and ranchers I know spend a good amount of time avoiding: Bankers, lawyers, environmentalists and consultants. Though I have always considered myself to be a “rancher” first, I am really now delving in the field of being a “consultant”, trying to spread some friendly warnings about some of the pitfalls I have experienced and seen in my ranching career. My love for this industry is why I write it.

I hope you enjoy this short report.

Ryan

Ryan Copithorne
Cows in Control Inc.

Have No Business Plan or Strategy

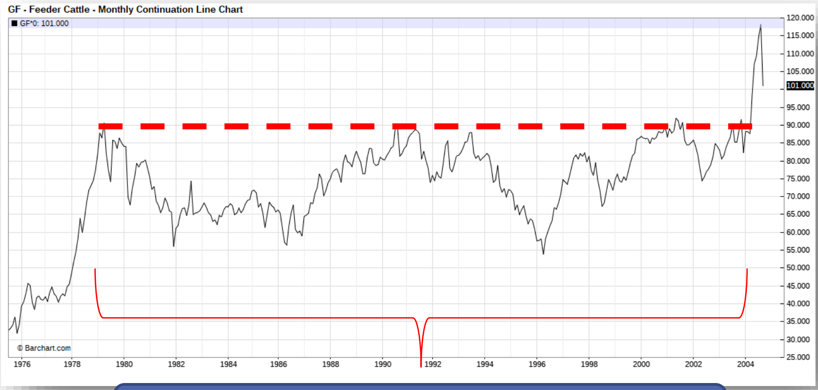
"It's not enough to just show up. You have to have a business plan."
CartoonStock.com

"There are two good years in the cattle industry, 1978 and next year". That is one of my favourite cattle industry jokes, because I see it so often. A rancher's natural tendency is always towards growth. That is, growing their numbers on anticipation of a market lift making them rich.

Ranchers in reality need to have a business plan that will work in an environment of flat commodity prices, or plainly, will make money even if the market doesn't go up. If calf or grain prices are the same as last year, will you be profitable?

Market rises are a windfall when they happen but should not be expected as part of your ranch strategy. From 1978 to 2004, cattle markets failed to make new highs. That was a 25-year period following the great boom in prices from 1973 to 1979. A lot of operations disappeared in that time period or were kept alive by subsidies alone. The ones that thrived were the ones that had a strategy for making money operating in a "flat" market.

From 1978 to 2004, no new highs were made in the market..



1978-2004 25 years of sideways markets

In fact it is quite typical in commodity markets after a boom in prices like we saw in 1978, to give back 50-60% of its recent gains, and then track sideways for a long period until a new catalyst comes along to push prices once again. This is what some people refer to as the "boom, bust and echo" of commodity cycles.

Whether you are starting out or mid-stream in your farm operations, to be successful, it is imperative to have a ***vision*** of where it is you are headed, and an ***action plan*** to get you there. What is it that you are trying to accomplish, and how do you plan on getting there?

"Steppingstones" are needed to get you to your destination that can be measured and monitored for progress. Some people use **SMART** goals (specific, measurable, achievable, realistic, and time focused) as these steppingstones.

A strategy is required for each of the following categories:

Land: to rent or to own? Is this the right land? What kind of returns can I expect on this land? Can I afford it?

Labour: Who is going to look after the day to day? How many employees?
Assets: What kind of equipment do I need and what can the operations afford?
Feed: Do I produce or buy feed? Is feed plentiful near me? Type of feed?
Cattle/Crops: What type of cattle do I need to run to be profitable? Custom or Owned? What is the marketing plan? Genetics Plan? What type of crops grow best here?
Finance: debt or equity? To what levels of each is acceptable?

We will not go into detail on these items. I only wish to highlight that to be successful, a larger vision of what we are trying to achieve with the entire operation, and action plans with SMART goals for each of these categories are needed to ensure we arrive at the vision. For each of the categories, we should have a profit and loss analysis on them (example, don't hire employees or buy tractors that the cattle or grain crop can't afford!)

The quickest way to lose the family farm business is to have no direction on where it is headed besides growth at all costs and waiting for the "Big one", that one in 25 year cycle high in prices. This leads into our next way to lose the family farm…

Grow Your Volume When You Don't Have Margin

Most ranchers measure wealth in number of cows and success in how nice the cows look. For grain farmers, it is the number of acres farmed and the gloss on the equipment. Money is abhorred. As soon as a rancher or farmer gets money or access to money what do they do? Go out and buy more cows, more acres, or worse yet, depreciating assets, instead of saving funds, reducing debt, or investing in ways to lower costs.

Growth of the herd should be based on profitability, not on programmed growth. Dreams of a "retire early" market move coming may leave you a very old dreamer and late retiree. The idea of being the biggest rancher or farmer in your community could drive you to being the biggest debtor in the community. If cattle or grain acres don't work on a small scale from a profit perspective, having more of them won't help. It will actually accelerate your downfall.

Scale is important to cover your overhead expenses which we will later discuss, but if you don't have a low cost operating structure that works whether you are large or small, then the bigger you get, the harder it will be to survive the lean years and debt will accumulate.

A good way to lose the family farm is growing your herd or acres unprofitably for years on end. That leads us into our next method to blow the family farm…

Take on Debt

Albert Einstein has a famous quote about money:

> *"Compound Interest is the eighth wonder of the world. He who understands it, earns it. He who doesn't, pays it"*

In any small town, the fanciest buildings in town are the insurance salesman and the banks (In fact, banks have actually started downplaying their buildings to try to counter the image.) The reason for the wealth is compound interest. 5% interest when allowed to compound over time will either double your money in only 14 years if you are collecting, or double your debt in 14 years if you are paying! Some call it the rule of 72, the death knell to debtors.

THE RULE OF 72

Estimates how long it will take for compound interest to double your money	Annual Interest Rate	Rule of 72	Years to Double
	4%	72 ÷ 4 =	18.0
	5%	72 ÷ 5 =	14.4
	6%	72 ÷ 6 =	12.0
	7%	72 ÷ 7 =	10.3
	8%	72 ÷ 8 =	9.0

NOTE: The Rule of 72 is a mathematical illustration. Interest rates may fluctuate and are dependent upon many factors, such as type and risks of a particular investment, economic and political environments, etc. No graph or chart can accurately predict rates of return.

What is even worse is if you are borrowing the money to pay your interest off. Then not only is the interest compounding, but the interest on the interest is compounding, and your debt begins to go exponential.

Margins on your operation need to exceed the interest rate or you are going backwards. If you have mortgage debt on your land, financing livestock or equipment, and have a government cash advance on your operating expenses, first of all you may be in trouble, secondly, you will need to make sure that you are properly accounting for your interest expense and the compounding effect of interest on your long term profitability.

It has been my experience that the standard custom operating rates we often quote in our industry don't include principle and interest payments in that calculation. Those with equity only (own the cows/equipment and the land) are the ones that set the rental rates and custom operating rates. Those with debt laden operations generally cannot operate profitably at these rates as compared to one who has no debt.

It has also been my experience that to be competitive, many people generally cannot afford to pay rent. They do better on land that is owned where the value the cow is adding to the land or the inputs a farmer puts into the land is captured. Captured not only from a biological sense (manure fertilization, residue, weed control etc.) but also financially (grazing/crop yield income).

To lose the farm, you need only let the debt get to a level where the compounding interest is higher than your 10-year average returns and you will automatically begin to slide to oblivion. Easy as that! Speaking of not tracking things, that is our next tip to blowing the ranch…

Underestimate or Not Value Overhead Expenses

Land		
	Land rent attributed to cattle	$ 5,000
	Pasture improvements	$ 1,000
	Property tax	$ 3,750
	Office expenses	$ 500
	Fence repairs/ improvements	$ 1,000
	Water repairs/improvements	$ 500
	Building repairs/improvement	$ 500
Labour		
	Winter Custom Labour costs	$ -
	Summer Custom Labour costs	$ -
	Full time Labour costs	$ 60,000
	Administration/management	$ 15,000
	Accounting/tax prep	$ 1,500
	Conferences/travel	$ 1,000
Equipment		
	Equipment lease/finance costs	$ 5,000
	Owned equipment amortizatic	$ 5,000
	Equipment Insurance	$ 1,500
	Repairs	$ 500
	Fuel/oil/grease	$ 5,500
Feed		
	Feed hauling costs	$ 3,700
	Feed storage costs	

Cattle		
	Cattle hauling costs	$ 3,750
	Cattle checkoffs/commissions	$ 1,250
	Veterinary expenses/supplies	$ 5,250
	Hedge costs	$ 5,500
	Cattle software	
Utilities		
	Electrical utilities	$ 4,800
	Natural gas	$ 4,800
	Other (ex: solar, wind)	
	Phone/cell/internet	$ 600
Banking/finance		
	Principle due	$ 5,000
	Interest	$ 4,500
	Bank charges	$ 600
Other		
	Liability Insurance	$ 5,000
	general livestock	$ -
	taxes	$ -
	misc.	$ -

		# of head	# of days on Ranch/farm
Bred Cows		250	365
Bred heifers			
Weaned Calves			
	steers	115	60
	heifers	115	60
Yearlings			
	steers	50	150
	heifers		
	group 3		
	group 4		
	group 5		
Cull cows			
Bulls		10	365
Total Cattle fed days:			116,200

Total Overheads per Animal per $1.31 /animal/day

The best way to lose the farm is not account for your expenses until the expenses overwhelm you. This is the dreaded "overhead" expense or "yardage" as it is often called. These are expenses outside of direct operating expenses, the ones that keep costing you month to month no matter how many cattle or grain acres you are operating.

The big-ticket items on overheads are land costs, labour, building and utility expenses, and debt and finance costs.

As an illustration, feedlots that operate 10 to 20,000 head of cattle can get "overheads" down to 30-40 cents per head per day. In my analysis of multiple ranch operations, finding a ranch with overheads below $1/animal/day is extremely rare, and many ranches are $2-3/head/day.

When I ask people what their grass and wintering costs are on their cattle operations, they usually give the standard answer "Oh, $1.25/head/day for grass and $2.50/day for winter feeding" Assuming overheads alone are over $1/head/day, and the cost of feed alone these days is $2-3/head per day, these standard costs everyone is charging their livestock are completely out to lunch! The same is true on the grain side and all businesses for that matter.

I see this all the time and struggled with it in my own operations. Especially when you are using debt and renting land. Interest and rent can easily double your overhead expense.

Does it really cost just $700 to raise a calf to weaning on 200 cows or $3 a bushel to grow barley when the operator is driving a $70,000 pickup truck, has new tractors and equipment in the yard, a hired man with a house and pick up and $200,000 in debt not accounted for? "Back of the napkin" operating expense calculations are great in a pinch but can kill an operation if not fully loading overheads over time.

Each of us do the back of the napkin calculations to determine whether it makes sense to buy cattle or take on land. The best way to lose the farm is to forget to calculate those overhead costs. Let's talk about another thing that producers are notorious for by default…

Buy Retail, Sell Wholesale

As a rancher, it is easy to feel quite popular when around input suppliers. God bless them, we need them, but we are the low hanging fruit for retail suppliers. Everyone wants to market to the producer for large "markups" (profit margin) because we are so numerous, fractionated, and have no negotiating power unlike a large feedlot, packer, or grain processor.

We buy our inputs like tractors, trucks, drugs, chemicals, fertilizer and equipment with 15-45% margins and sell our product (livestock or grain) through an auction at wholesale commodity price levels. That is a dang poor business model!

Even worse, a common sight is to see producers going to purebred sales and paying exorbitant purebred prices for their bulls and replacement heifers only to bring them home and run them as commercial cattle, selling the offspring at commercial valuations. Have you ever done the math on buying a $3000 bred heifer when you are only bringing $100/head profits on her commercial calves each year? It doesn't work.

Ranchers and farmers are the most numerous segment of the supply chain and by far the most disorganized when it comes to buying and selling. They are price takers on the buy side and the sell side.

To lose the farm or ranch, buy high markup inputs, lots of them, and sell your product through auction marts or elevators at commodity wholesale prices. We can accelerate the damage with the following…

Have No Risk Management Plan

Cattle and grain markets can move upwards of 20%, up and down in the course of any given year. For example, on $1000 calves, that is $200/calf in simple market price gyrations through the course of a year. What a roller coaster!

I will focus on cattle here in this illustration, but the concepts apply to grains and other livestock as well.

From 2015-2016 calf prices dropped from over $3/lb to $1.80/lb in Canada, over 50% of the calf's value was lost in just one year, or over $600/calf in lost value!

Now, what can you do on your operations, be it grass management, genetic improvement, increasing weaning weights or elsewise that is worth $600/calf? If you added 50 lbs of weaning weight to every one of your calves which would be an accomplishment, that is only $100-150/calf.

Market moves can wipe out a whole years' worth of operational improvements and hard work from a financial standpoint leaving you scratching your head at what you spent the whole year doing?!

Using price risk tools to secure higher prices for your cattle, no matter when you sell…

Ranchers generally wean at the same time and sell their calves around the same time, shall we say October 26th, the peak of the fall run each year? If you have good calves you can get 5 or 10 cents per pound over the market average. What about getting 50 cents or a dollar a pound over market by pricing your calves at a time of year when prices are topping?

Or farmers will deliver their crops to the elevators at harvest time. If they store grain, they may make a few cents more a bushel. What about making 20 or 30% more by pricing the grain ahead of time in the spring rallies or other market highs through the course of a year?

There are many tools for risk management. There is insurance, futures, options, forward contracts and even retained ownership or storing grain to wait for a better market. You can use these tools to “lock in” your prices at the highs even if nature and your operation dictate that you deliver calves or grain in the fall, the same as everyone else.

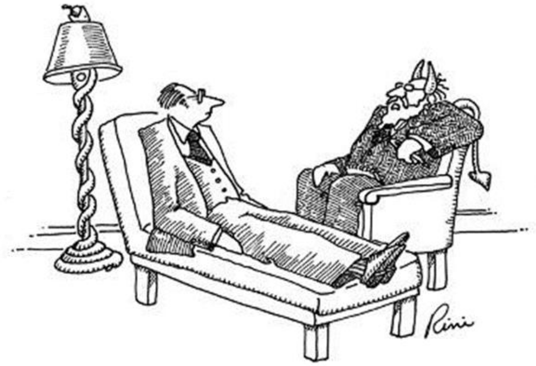
A good way to lose the farm is to ignore these tools and market your product at the same time as everyone else, being whipsawed year to year with 20+% market moves that negate all the hard work you do each year to add value.

Buy High, Sell Low

A classic way to blow the farm is to overpay at the top of the market cycle, paying top dollar when everyone including and especially the banker thinks the market is going to rise indefinitely, only to find the market gets cut in half a year later, and your banker now changes his mind and calls your loan.

I have seen bred cows trade for $700 and the same cow trade for $3000 a few years later. Perhaps a year or two after that she is back down to $1000. That is the commodity business for you!

The famous investor Warren Buffett says, "*be greedy when others are fearful, and fearful when others are greedy*". This applies to buying and selling cattle or land. When no one wants to own a cow or farm another acre, that is usually the time to buy them, when the auction barn is empty of people and full of cattle, or the coffee shops are full of stories of gloom. When you see sale barns full of people, and rapid fire bidding, eat the free steak dinner and go home, don't bid!



"Dare to be different! Any wimp can buy low and sell high."

Bankers are notorious for handing out umbrellas on sunny days and taking them back when it rains. A sure way to lose the farm is to borrow heavily from your enthusiastic banker to buy at the tops of the market and be forced to liquidate in a drought or a depressed market on account of your now schizophrenic banker who has lost all his enthusiasm. This method of losing the farm is similar to the next method…

Do What Everyone Else is Doing

"The soft minded man always fears change. He feels security in the status quo, and he has an almost morbid fear of the new. For him, the greatest pain is the pain of a new idea." - Martin Luther King Jr.

We have already discussed how ranchers generally sell at the same time of year. Have you noticed that the calves are looking more and more similar each year? We are in a commodity business, and it seems that producers are trying to "commoditize" their commodity even further by making their cattle exactly the same as everyone else's. Now this is good and bad. We need uniform quality of product from a consumer standpoint, but uniform quality doesn't have to mean "all the same". Think of wine. Would you like if there was only one type of wine? Or one flavor of gum? If ranchers are all doing the exact same thing, then all we can expect is zero margins. Why would I pay one rancher more than another for his calves if they are both producing the same product? It is a zero sum game.

Have you heard people say at industry meetings "the industry needs to do this…" or "we as an industry need to do that…"? The secret to making money is to differentiate yourself from what everyone else in the industry is doing, and then convince the crowd followers that your idea is the one they should be following. Don't do what the "industry" does.

Why do farmers only grow three or four different types of crops? Why are most cattle Angus crossed these days? Why are we implanting cattle when the consumer doesn't want implants? The world is not short of beef, otherwise the business would be better.

Admittedly, niche market and "ranch to retail" programs have been a disaster. Very few of them have succeeded. However, is our commodity style "industry" approach any better? I see the average age of the farmer getting older and older, young people are leaving the business. The "industry" needs a facelift. We need new ideas! Stop doing what our grand parents did, or what the "industry" recommends, we need to innovate!

The surest way to blow the farm is to operate with zero margins. The sure way to operate at zero margin is to overproduce the exact same thing as thousands of your neighbours are producing.

Misuse Your Land

The greatest resource a rancher or farmer has is the soil he/she stands on. It is the resource that creates the crops and pounds of beef to be harvested. The quickest way to blow the farm is to either abuse the resource, or not understand it properly.

The soil is a bank of nutrients, microflora, microfauna, and composting organic material, all necessary for plant growth. Without going into detail, we are either adding to the bank or taking away from it. Proper grass and crop management allows for organic material to go back into the soil and create healthy plant and root systems that put carbon into the soil. That is adding to the bank. Skinning off the ground or overcropping without returning nutrients will create a desert over time. Just ask the former farmers of the Sahara region, or even many parts of the central states that at one time were farmed and are now dust bowls.

Maximizing cattle numbers or crop yield at the expense of your soil resource is a losing game.

The other way of misusing land is to not understand its best purpose. Trying to grow high value, high volume crops on poor soils is an example. Some lands should never be farmed. Ranching or farming on high value lands next to urban centres is another difficult game of which I am all too familiar. Consider the overhead costs of land that is many thousands of dollars per acre due to its recreational value. Compare this to more rural lands where grasslands are still valued at agricultural rates. If an acre of land is more expensive than a calf, then cattle should not be your primary source of income on that land.

What often happens on expensive land is that your ability to borrow money increases, and you pour debt money into your uncompetitive ranch/farm in an effort to make it competitive with lower cost operations. A losing game and a sure way to blow the farm.

Have No Succession Plan

"That someday has arrived son - it's all yours."

"Why do I need succession planning? I'm very alert, I'm very vibrant. I have no intention to retire." - Sheldon Adelson, 85 years old, CEO of Las Vegas Sands. Hmm, we'll see…

I shudder at all the ranches and farms broke up through the ages on account of having no succession planning. The family gets into a war over the assets upon the death of the owner, or worse yet, the tax man walks away with half of it. Succession planning is more than just "who is getting what when I die". It is developing strategies to avoid tax, determining the future direction of the operation and who will run it, and allocating and protecting multiple potential stakeholders.

Another thing so prevalent is 60 year old men working for their 85 year old fathers, having never managed anything, only serving as “muscle” for the old man. When the father finally passes on, the son has no knowledge of management and the farm fails.

I asked a banker friend of mine one time, “what is the secret of success in multigenerational operations that last beyond the third generation?”. His answer without hesitation was “third party management”. That doesn’t mean that families have to turn over the operation to outsiders entirely, but it does mean that there should be some level of objective standards and third party oversight when determining how businesses are run so that they are not subject to the emotional rollercoaster of family disputes.

To blow the family farm, chase the younger innovative fresh minds away from the operation, do all the work yourself until you can hardly walk or get injured, and have no one that understands your business to follow you up. When you pass on, let the accountants and lawyers divide your estate into uneconomical bits and pieces, with the government getting the largest share. Delay and do not discuss the future with the younger generation, frustrate them until they leave. This is a great way to blow a farm and very prevalent.

Think too Highly of Yourself

If you make yourself irreplaceable on the farm or ranch, you will be irreplaceable. You will never get to have a holiday, and will burn yourself out, ultimately blowing the farm.

Likewise, if you tie the success or failure of the operation to your sole management of it, then when the business failures and successes fluctuate up and down with every market cycle, so will your emotional state of being. It is a rollercoaster tying your emotional state of mind with the ebb and flow of business and is why mental health issues on farms is now being talked about. ***The business should not be your identity***.

For longevity, a person has to be able to laugh in times of trouble as well as good times. Someone geared towards longevity must never take themselves too seriously and realize that there are things that are simply beyond our control sometimes. Someone focused on longevity will not focus on the uncontrollable, but rather target the things they know they can influence and surround themselves with people who can help.

We talk about the garbage shows kids watch these days, but really, one of the worst influences of the past 100 years came from the old western movies. A lone cowboy shooting up the town singlehandedly, eliminating anyone who he disagrees with, executing his own form of justice, and riding off alone.

The John Wayne culture is alive and well in ranchers and farmers alike, bolstering themselves in their independence rather than celebrating collaboration and cooperation. Three farmers in one area, each with their own line of equipment, each operation too small to afford the equipment they own, but they are too proud to collaborate and share equipment. Fragmented cattle producers with no independent negotiating power, marketing part loads, part pens of cattle at discounts when if they teamed up with a neighbor to fill a pen or a truck they could exact a premium for their cattle. Enough said.

A good way to blow the farm is to make yourself irreplaceable, tie your identity to your operation, be completely independent and uncollaborative.

Conclusion

I hope that you were able to look at this piece lightheartedly, laugh a bit at the absurd behaviours we all seem to have a little bit of, and that this booklet might generate some thoughts for you that will ensure the longevity of your operation. I have made many of these mistakes myself and see it so prevalently in the ranching and farming industry, I couldn't help but write this little satire.

A few years back, I developed a company called Cows in Control Inc. to assist ranchers in overcoming some of these issues as I saw so many people battling with them. The company is designed to serve and work with producers and family farm businesses to find solutions.

Cows in Control works with producers to do the following:

- ✓ Develop strategies for livestock
- ✓ Assist with market timing and strategy
- ✓ Help ranchers with price risk management
- ✓ Bring ranchers together to collaborate on the buying and selling of livestock
- ✓ Keep ranchers informed of what is happening in the marketplace
- ✓ Network producers with succession planners, brokers, banks, feedlots, packers, etc.

Give us a call if we can be of assistance to you, God Bless!

COWS IN CONTROL Inc.

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Ryan Copithorne's career has involved managing and operating a historic family ranch and farm, as well as designing and building one of Canada's largest cow/calf programs as Cattle Director for an investor owned multi-ranch operation with 8500 head of cattle. He also worked in the cattle feeding sector with a privately-owned cattle feeding, grain trading and consulting company and currently owns a ranching operation and consulting company west of Calgary. Ryan has an MBA from Queen's School of Business, a finance degree, and over 25 years in the ranching and farming business, including over 20 years of commodity hedging experience. He currently is the president of Cows in Control Inc., a company designed to assist ranchers with the issues discussed in this book.

Cover and Back Photos Courtesy of Lee Gunderson