

What to do with profits?

Surviving High Prices Webinar Series

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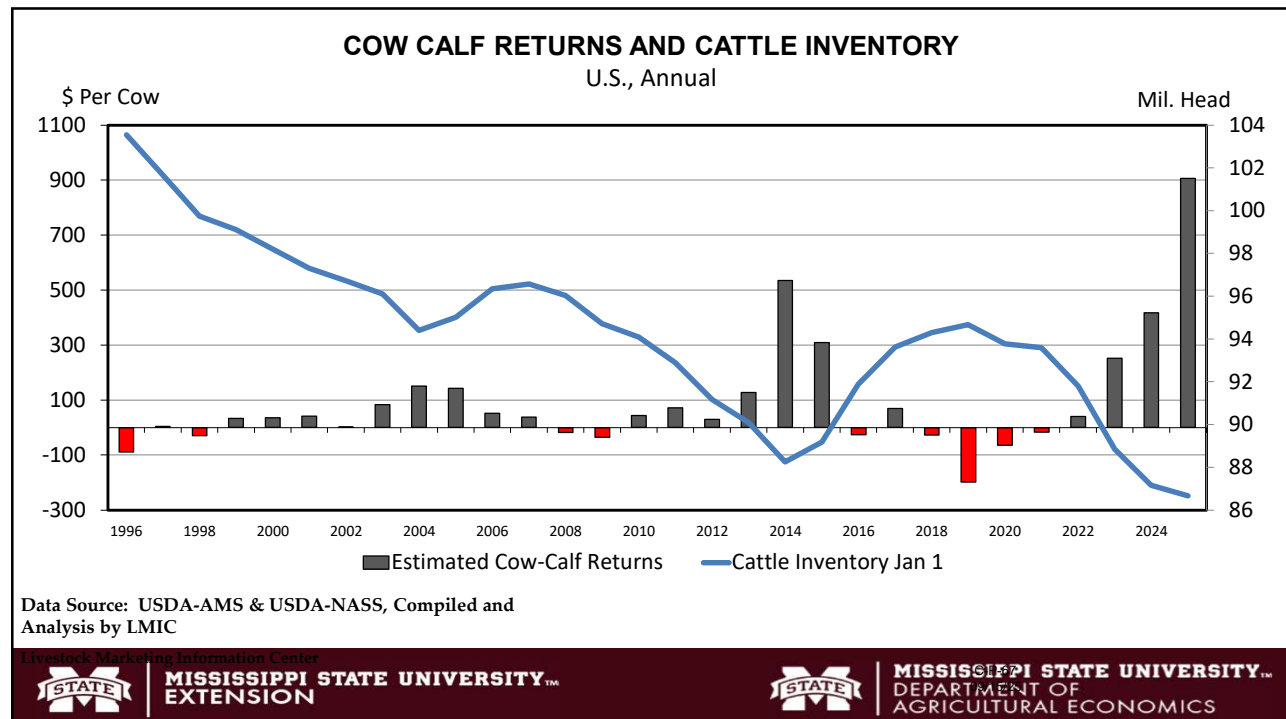


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What to do, or not do with high prices?

- Purchasing equipment
- Improving herd efficiency
- Forage production investments
- Farm financial health



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Purchasing Equipment

- Incentive to purchase equipment to reduce tax obligations
 - Can be a valid option to reduce taxes
 - But should not be the sole reason for buying
- Tax benefits are relatively short-term but equipment is a long-term investment
 - Still have to pay off loan when prices decrease
 - Tax benefits less when prices are low



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Purchasing Equipment

- New equipment can increase costs of production
 - Increases break-even price
 - Can make it harder to be profitable when prices fall
- Determine how buying equipment will impact costs of production and/or revenue
- Want to buy equipment to become more efficient
 - Decrease costs
 - Increase revenue



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Machine Cost Calculations

- Machine cost calculations allow for determining how much it costs to run a given piece of equipment
- Broken into two types of costs:
 - Ownership costs (Fixed costs)
 - Operating costs (Variable costs)
- Typically break-down costs to per hour or per acre basis
- Developed by ag engineers and ag economists
 - ASABE Standards



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Machine Cost Calculations

- Farm equipment typically second-largest investment for farm after land
- Complex to determine annual costs for equipment
- Can be used to determine Custom Rates
- Tool available
at: <https://www.agecon.msstate.edu/whatwedo/budgets.php>



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Machine Cost Example

	Old Tractor 2015	New Tractor 2025	
Size	2WD 75	2WD 75	Change
Purchase Price	\$35,000	\$60,100	\$25,100
Annual use (hours)	400	400	-
Operating Costs \$/hr	\$29.29	\$31.72	\$2.43
Ownership Costs \$/hr	\$7.20	\$16.55	\$9.35
Total Costs \$/hr	\$36.49	\$48.27	\$11.78
Total Costs \$/yr	\$14,596	\$19,308	\$4,712
Herd size	50	50	-
Total Costs \$/cow/yr	\$291.92	\$386.16	\$94.24



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Machine Cost Calculations

- The new tractor increased costs
 - Break-even price is now higher
 - More risk when prices fall
- But what if you are able to buy equipment that allows you to do an activity faster?
 - Ex. New hay cutter



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Machine Cost Example – Hay Cutter

	Old Mower	New Rotary Mower	
Size	8'	10'	Change
Purchase Price	\$15,500	\$17,400	\$1,900
Annual use (hours)	100	100	0
Operating Costs \$/hr	\$13.32	\$17.61	\$4.29
Ownership Costs \$/hr	\$16.66	\$23.30	\$6.64
Total Costs \$/hr	\$29.98	\$40.91	\$10.93
Field Capacity ac/hr	3.9	6.8	2.9
Total Costs \$/ac	\$7.69	\$6.02	-\$1.67



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Purchasing Equipment

- Buying equipment can pay if it makes you more efficient
 - Takes less time to do activity
 - Old equipment breaks down a lot
 - Reduces hay losses
- But it can also make break-even price higher
- Don't want to set yourself up to fail when prices fall
 - Prices always come down



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Improving Herd Efficiency

- Improving herd efficiency can be a beneficial avenue to increase profitability
- Cull less productive cows
 - Cows that produce a lower value calf
 - Calves outside desired calving window
 - Doesn't match rest of the herd
- Goal is to improve uniformity
 - More uniform calves in weight and color can increase sales price
- Cull cows have higher value now than when prices fall



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Improving Herd Efficiency

- Investing in Artificial Insemination can help improve herd efficiency
- AI offers numerous advantages to even small producers
 - Access to superior genetics at a reduced cost
 - Heavier weaning weights/better replacements
 - More uniformity
 - Tighter calving interval
 - Improved conception rates
 - Reduced bull requirements



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25 Head Example

	Natural Service	AI
Cows	25	25
Pregnancy Rate	90%	95%
Replacement Heifers (per year)	3	3
Steers sold	12	12
Steer weight	550	575
Steer price	\$2.90	\$2.90
Heifers sold	8	9
Heifer weight	535	560
Heifer Price	\$2.45	\$2.45
Revenue	\$29,626.00	\$32,358.00
Bull Costs	\$2,290	\$2,290
AI	\$0.00	\$2,263.17
Net Returns	\$27,336.43	\$27,805.26
Change in NR from AI		\$468.83



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Farm Financial Health

- No wrong time to evaluate farm's financial health
 - Enterprise Budget, Balance Sheet, Cash Flow, Income Statement
- Any decision a farmer makes has a financial component to it
- Need to know how bank evaluates operation
 - How does it impact how the bank views my farm?
- How does it affect my long-term financial goals?



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Overview

- High price environments allow for reinvesting in the business
- Make sure you're not setting yourself up to fail when prices fall
- Increased efficiency will make the farm more resilient
- Understanding the farm's financial situation and how those investments impact your financial ratios is key



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Thank You! Questions?

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