Business shock absorbers can assist with managing climatic variability

Climatic variability is here to stay and many scientists predict it is likely to increase. Regardless of your personal perspective on climate change, the need to manage climatic variability should be embedded into your farm business strategy.

Climatic variability presents itself to us in the form of production shocks. These production shocks could include:

- Extended periods of low rainfall or drought
- Failed springs
- Late breaks
- Heat shocks or heat stress
- Cold shocks or frost
- Extreme rainfall events
- Floods
- Fire
- Commodity price variability
- Input cost variability

To effectively manage the consequences of production shocks, it is important to establish resilient farm business models that can bounce back quickly. Embedding shock absorbers into your business is one way to increase the resilience of your farm business.

WHAT ARE BUSINESS SHOCK ABSORBERS?

Business shock absorbers can come in a variety of forms, including:

- Farm management deposits
- Cash reserves
- On farm reserves of low cost, high quality fodder
- Stop:Go points in your grazing management strategy which allow you to destock in a proactive rather than reactive manner
- Excellence in production management
- Well considered enterprise selection to match production environment
- Low cost of production
- Low overhead cost structures
- High equity
- Well considered stocking rates with an ability to ‘flex’ stocking rate to match seasonal conditions
- Developing feed wedges in autumn and/or spring to assist with managing the winter and summer gazing periods
- Adequate insurance

Having business shock absorbers in place can position a farm business well in times of adversity and increase business resilience. They can also have an enormous positive impact on the mindset of the management team following a production shock.

CASH RESERVES

Farm Management Deposits or cash reserves within a business provides an immediate source of capital and cash flow if needed after a production shock. Access to such capital can increase choices after or during a production shock. They can also save the business from having to increase core debt, which could have a detrimental impact on the long term viability of a business.

FODDER RESERVES

The 2006 and 2007 droughts tested many southern grazing businesses, as a result of the combination of record low rainfall and record high prices for fodder and grain. This left a lasting impact on all who fed stock through this very difficult period. Many livestock producers responded by incrementally establishing low cost, high quality fodder reserves to draw on in the future if and when needed. One strategy adopted by some livestock producers was burying largesquare bales of silage in underground bunkers.

STOP:GO POINTS

Proactive rather than reactive management will always pay dividends in grazing businesses. Regular monitoring of feed on offer, grazing budgets and seasonal outlook provide scope to ensure you are able to proactively manage changing seasonal conditions (see module 8 in the *Making More From Sheep* manual for assistance with understanding your whole farm feed supply, knowing your animal demand, matching supply to demand and tools for monitoring your progress). When assessing feed on offer it is important to recognise that frequency will always trump accuracy. A strategy employed by some grazing businesses is to always have 120 days of feed ahead of them. If seasonal conditions deteriorate and they have fewer than 120 days of feed in their pastures, they start destocking until they are back in a positon where they have fewer stock numbers but still 120 days of feed.

EXCELLENCE IN PRODUCTION MANAGEMENT

Excellence in production management is an effective business shock absorber. Excellent production managers are capable of generating superior results in all seasons. They are able to leverage more income from the same level of inputs. Essentially this results in a business that is retaining a greater percentage of gross income as net profit before tax. Farming businesses at the top end of agriculture are able to consistently retain more than 30 per cent of turnover as net profit before tax. This means that these businesses could face a production shock that reduces gross income by 30 per cent and still break even or maintain modest levels of profitability. In comparison, for a business that is only retaining 10 per cent of gross income as net profit before tax, a 30 per cent reduction in gross income would leave them with a significant financial loss.

Top performing farm businesses are achieving excellent results through a combination of increased productivity per hectare and developing low overhead cost business models. High performing farm businesses tend to also be very good at matching land type to enterprise selection by understanding the highest and best land use for their properties.

LOW OVERHEAD COST STRUCTURES

It is very difficult to be a top 20 per cent producer for farm profitability and performance without having a low overhead cost business model. It is not uncommon for the most profitable farm businesses to have overhead costs per hectare that are 30 per cent lower than their peers.

Low overhead cost business models also result in a lower cost of production. Businesses that have a low cost of production are more resilient. They are more resilient because they produce increased levels of profitability in all years and they can also maintain profitability at times when commodity pricing is lower.

Having high levels of business equity and low or very serviceable levels of business debt also provides an increased level of choice in times of adversity. Adequate insurances for extreme events such as fire and hail also increase business resilience. Early 2014 was characterised by some long-running heat waves in some regions across Australia. These conditions created perfect conditions for bush fires and some properties lost all of their feed base and fencing infrastructure. This certainly tested the adequacy of some growers' insurance policies, particularly for refencing at full replacement cost.

WELL-CONSIDERED STOCKING RATES

Successfully maintaining higher stocking rates in a sustainable manner requires systems thinking. It is important to understand and remember that profitability is maximised when stocking rate is optimised. Pushing stocking rate beyond optimal stocking rates for your property, your management and you environment will be detrimental to business performance and the sustainability of the production system. Well-considered stocking rates, combined with a capacity to adjust or flex stocking rate according to seasonal conditions, become an effective business shock absorber within a grazing business.

Stocking rate can be flexed either by having livestock classes that can be quickly and easily off-loaded when seasonal trigger points are reached or by having grain crops that can be sacrificed and grazed rather than harvested. Winter and summer carrying capacity can be enhanced by building feed wedges in autumn and spring. An autumn feed wedge can be created by using containment feeding or by resting a paddock the previous spring then grazing it in early autumn while other grazing paddocks get away.

Using a combination of these business shock absorbers, it is possible to develop a grazing business with increased resilience and a greater capacity to manage climatic variability. The level of business shock absorbers employed by a farm business will depend on the level of climatic variability common to your region and your personal risk profile. The greater climatic variability in your farming region, the greater the need for incorporating business shock absorbers into your business model.

Contact:

Simon Vogt

Rural Directions

Phone: 0407 959 836

Email:SVogt@ruraldirections.com

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More Lambs More Often, contact:

Dr Andrew Thompson

Phone: 0437 316 117

Email: andrew.thompson@at-consulting.com.au