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FOR IRRIGATION CROPPERS

Planning for profit in challenging times

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PLANNING FOR PROFIT IN CHALLENGING TIMES

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OVERVIEW

- Understand the meaning of sustainable profit – navel gazing at annual profits alone will constrain the ability of your farm business to survive in the longer term;
 - There is no new way of creating profit for a farm business – rather a reliance upon 4 tried and tested principles;
 - Address the 4 key principles of profit and understand the implications each of these parameters has on short term EBIT growth, and longer term investment health;
 - There are strategies that manipulate the principles for better effect – successful farmers manage the core principles of profit and therefore sit in the driver seat of a sustainable business.
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Viability v Sustainability

Business managers, regardless of what industry they are in accept the realities of declining terms of trade. In devising planning actions and adjustments' to maximize business profits, farm managers have to comprehend the principles that create and then sustain real income.

Do not get business viability and sustainability mixed up. There often seems to be a level of comfort attached to viability – it is not enough as it is generally “surviving” from one boom to the next.

Viability refers to the business' capacity to meet financial commitments and amble from year to year. Essentially this is avoiding foreclosure.

Sustainability is the capacity to shock absorb if required and continue to progress the business, to provide its proprietors with a worthy salary and lifestyle whilst engendering a sense of wellbeing and confidence for the future.

Annual profits make Christmas dinner tastier, but it is important to also understand your investment such that you know where the business is heading in the longer term.

In reality does anyone achieve solid and consistent annual profits? If you know and understand where you and the business are going then all of your decisions will reflect that 'future' aspiration and hasten its outcome.

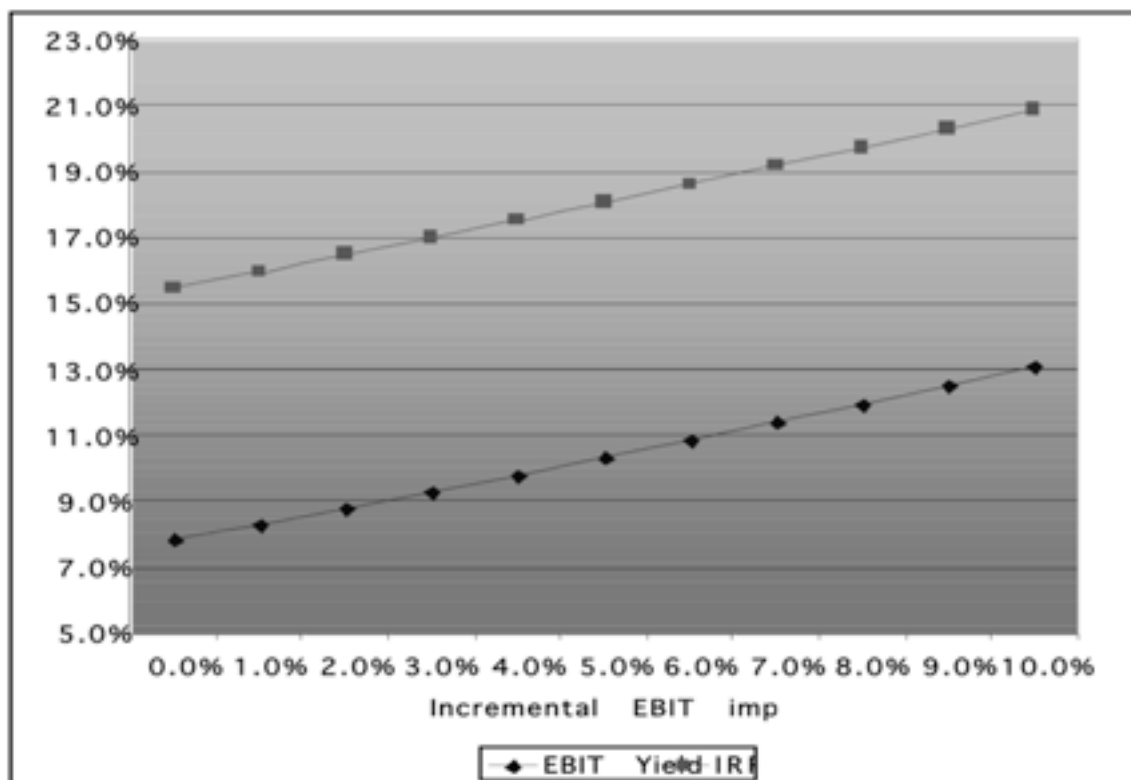
Sustainability Drivers

The 4 key principles of planning for sustainable profit are:

1. **Productivity**
2. **Cost control**
3. **Control of prices received**
4. **Scale of business**

The order of priority as to how each principle is addressed is entirely dependant upon the positioning of the business in its cycle of growth, the stage of evolution of the proprietors needs and the proficiency of management.

For the business savvy farm manager there is a strong correlation in agribusiness between incremental increases in annual profit and longer term investment health.



When there are constraints inhibiting profit, leading agribusiness managers will reassess and strategise to improve the 4 key principles of creating sustainable profit.

Included below are some of the Booth Associate client strategies that have proven effective in addressing profit constraints.

Productivity

- Keep pushing the business to improve output. You should be forgiven for navel gazing at the Christmas table. Continue to seek production benchmarks from industry and challenge the management team to match and beat them;
- Create Water Use Efficiency benchmarks and better them each year. It is relative to water supply even though drought creates limitations on water supply. It is therefore imperative to make more from the water you do get, whether you are an irrigator or not;
- Understand core competencies of management to concentrate upon increasing yield benchmarks in the primary enterprises;
- Surround the business in support when venturing into alternative investments to minimise risk and to encourage external/ unbiased critique;
- Focus on quality as well as quantity.

Cost Control

- Understand the limiting resources within the business (water and capital, water and capital...) and calculate the best returns for that resource;
- Maintain currency with looming financial year profits – start assessing potential profit in say February/ March each year and drive them back into the business to improve future productivity, increase scale or diversify the investment portfolio to spread risk;
- Where possible turn capex into opex. Don't forsake cashflow in the business but don't make tax a significant cost to your business. A business starved of cashflow has undue pressure and this can test relationships with suppliers and financiers.

Control of Prices Received

- Increase the value of farm outputs by creating relationships and contracts with end users;
- Seek advice from a range of credible sources;
- Use forward sales and derivative products strategically to create prices you are comfortable with, however...
- If you don't think you can produce it - don't sell it.
- If you don't understand derivative products, and don't have time or someone credible to keep an eye on them for you – don't use them.

Scale of Business

- Embrace growth but understand the risk – the business can not stand still or it will go backwards;
- If increasing scale, plan ahead with sensitivities. Understand the ramifications of fluctuating parameters of rainfall, water allocation, yield, increasing and decreasing costs and prices – understand the risk and the reversibility of decisions;
- Lack of capital?? Stratify assets – find someone else who is happy to invest in land and/ or water and provide the management via lease/ share-farm etc.
- Understand the appreciation history of the investment – in an attempt to increase scale you may lease land and buy water as capital gain on water may be more likely??

Seek advice and therefore support to use sound investment appraisal techniques such as NPV & IRR analysis to accurately capture capital costs, future cashflow driven from the investment and capital out based upon the appreciation/ depreciation of the asset over the appraisal timeframe.

This will help you measure risk, and provide critique on whether you should send your hard earned money in that direction.

For a farm business to plan for profit and therefore be sustainable, the management team needs to continually improve on the 4 key principles highlighted in this summary paper.

Simply planning year-to-year may belie the longer term sustainability of your business.

Whilst many of his philosophies were off centre the following quote from Machiavelli is concise;

“I’m not interested in preserving the status quo; I want to overthrow it.”

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