

The Attractive Option of Staying Small and Highly Profitable



- The number of cows a farmer has is a poor measure of success. Larger farmers have generally succeeded financially. But being smaller, profitable and growing your business outside of the farm gate is equally successful. It may be that being smaller and happier is a great outcome.
- It seems to be a trait of human nature that no matter how many cows people have they think that those with more cows are greedy, and those with less are not as successful.

The importance of smaller herds to NZ

- Much of the cutting edge of farm management efficiency is driven by herds of less than 300 cows. Larger farms, as a generalisation, pick up the high efficiency tricks of the best smaller farmers and apply them at scale.
- Herds of less than 300 cows are very valuable to the NZ dairy industry in terms of their contribution to bovine genetic gain. The accuracy of their cow recording and information is generally substantially superior to the information from large herds. This is not commercially recognised by the industry. It is unfair that it is not recognised.
- Herds of less than 300 cows supply the majority of bulls entering AB companies.

Farm amalgamation is a commercial reality – but what does it mean for small towns?

- The small town of Ngatea and surrounding area (where we live), has changed markedly over the last 50 years.
- The town population has grown from 700 to 1500 people. The surrounding population has gone from 900 to 600. Combined, the population has grown from 1600 to 2100, but the town/farm split has gone from 1:2 to 3:2.

- The number of resident, non-farming professional/business people has gone from 40 to 15 over that period. While the number of shops remains the same, many are absentee-owned or services have gone. No postmaster, the two bank managers' positions have gone, the dairy factory manager position is gone, the district council amalgamated and no council CEO, engineer or surveyor, the two rural retailers sold to RD1 and Hammer Hardware, the chemist is now owned by a Hamilton chain, both services stations are owned by absentee chains etc.
- The amount of milk produced is three times higher from better farming techniques, better cow genetics, more developed land and more imported feed.
- The average farm has gone from one farmer and one single man milking 80 cows to three people milking 400 cows.
- The number of dairy farms in a 10k radius has gone from 120 to 40. After considering multi-farm ownership and absentee farm ownership, there are now only 25 farm owners living in the catchment.
- The leadership pool from farm owners and business professionals to operate schools, sports clubs, service clubs, churches etc has diminished from $40 + 120 = 160$, to $15 + 25 = 40$ over the fifty year period.
- The success of all community service amenities will have a strong correlation with the quality of the people in leadership positions.

Wealth creation in smaller farm businesses

- It is no less important to ensure wealth creation in small farm businesses than larger ones.
- The size of a sustainable dairy farm business will continue to increase in size. So if 150 cows are now the "basement" size farm without any outside income support, the sustainable size dairy farm will grow towards 200 cows over the next generation. However, there is nothing wrong at that point with still being happy milking your 150 cows, provided that there is economic contribution coming in from off-farm investment or income support from a partner working outside the farm gate.
- For farmers with smaller size farms, and wishing to grow their business, there are two options:
 - a. Use operating cash surpluses to grow into a bigger farm.
 - b. Stay with the smaller farm operation and use cash surpluses to grow the business outside the farm gate.
- Staying with a smaller farm but wishing to grow, there are several growth options:
 - a. Farm equity partnerships in NZ.
 - b. Farm equity partnerships outside NZ.
 - c. Some diversification into kiwifruit, beef, deer etc.
 - d. Commercial buildings.
 - e. Public stocks.

Small farms in cyclical downturns may have the advantages of:

- Having a lower debt leverage because they have gone through less debt funded growth phases.

- More diversified investments if cash surpluses have gone into other sectors, rather than buying another farm.
- Farm performance efficiency per hectare may be higher on smaller farms.

Wealth protection in cyclical downturns

- It is most important to understand your financial position well – very well.
- Understand what you are good at, and what you are not good at. Ask your partner, or a respected friend, or your accountant, what they think you are good at, and not so good at. If they think your weaknesses are different to what you think, they may not be wrong.
- Seek the best advice you can after you have understood your strengths and weaknesses. There is little point in seeking advice in the areas where you are strong. This, by human nature, may be the first place you look. It takes a discipline to avoid the “birds of a feather” approach.
- In serious downturns, work closely with all stakeholders. This includes bankers, staff and service providers. The messages will have subtle differences for each. But all must have the common threads of transparency, honesty and a demonstration of your own discipline.
- Be very disciplined in cost control in downturns. If you can hold that discipline into high return cycles, you go from being profitable to very profitable.

Some of the potential risks in staying a smaller size farmer

- If you are mainly rubbing shoulders with other small farmers, be careful not to get locked into “small think” to your detriment. Differentiate between small farms and “small think”. Larger farmers are more likely to be stimulated by associating with the more successful “movers and shakers”.
- If you are happy, and by choice locked into a smaller farm size future, be careful that in high income periods you are not over capitalising your smaller farm with feeding pads, sheds and “metal disease”. This is a real risk for a small farmer compared with someone wishing to grow who is putting their surpluses into appreciating assets (more land and cows), rather than depreciating assets (more buildings and machinery on the same land and with the same cows).
- Ensure your desire to operate a small farm is driven by choice to be a small farmer. Just check you are not saying that you want to be a small farmer when the real reason is that your level of farming efficiency means you have no option because you do not have the economic means to be a larger farmer.
- Finding a relief manager on a one-man 150 cow operation for a holiday or weekend off is more difficult than finding someone to relieve for anyone within a 600 cow unit. This is because the 150 cow reliever needs to understand everything on the farm, whereas the reliever within a 600 cow unit needs to be able to work as instructed by those in the operating system who are still on duty.

Staying small and thinking big

- Ensure you generate strong cash flows. Being small increases the need to farm efficiently.
- Optimise any off farm income opportunities. This may mean one partner working off farm. It may mean the farmer employing someone to do some of the lower returning farm jobs and working part time off farm.
- Ensure clarity around any off-farm investments and whether you want them to be cash generating investments (dividends) or value creating investments (capital gain). If your smaller farm needs income support in most years, then your attraction may be to cash generating investments. If for most years your small farm has you living comfortably then value creating assets may be more appropriate.
- Consider the timeframe you might desire with any external investment. This will determine the liquidity options that become important around your ability to exit.
- It is important to understand the risk versus return on any investments.

The attractive option of staying small and becoming highly and increasingly profitable

- Operating a 200 cow farm very efficiently should mean having a quality and comfortable living with cash surpluses to invest and grow outside the farm gate.
- Operating a 120 cow farm with some additional off-farm income should mean having a quality and comfortable living with cash surpluses to invest and grow outside the farm gate.
- If you are operating a smaller farm efficiently, and you are happy, and you are growing your farm business outside the farm gate, never, ever feel inferior to a large farm operator.

