



The opening module of *Making More From Sheep*, 'Plan for Success', focuses on setting objectives for sheep enterprises – an important component of this is working out and knowing your cost of production.

In 2009, MLA and AWI will be working together with consultants across Australia to deliver Managing Your Profit Drivers courses and to also introduce a new tool – the *Making More From Sheep* Cost of Production Calculator.

While the courses will draw on information available through *Making More From Sheep*, the new tool combines the MLA Lamb Cost of Production Calculator with the AWI wool equivalent into a single easy tool for sheep enterprises.

The courses will provide support to producers who want to calculate their cost of production, and then use this information to make business decisions.

Consultant James Hall, of JRL Hall & Co, says one of the key goals for a farm business and indeed at an enterprise level is to ensure that the cost of production of the commodity is lower than the price that one receives for the commodity when sold. This enables the business to produce profit.

"Another key aim of the business at each enterprise level should be a continual focus on means by which the business can lower their cost of production," he added.

"Lowering of the cost of production is necessary for longer term planning and profits to ensure the business can continue to manage the ever present declining terms of trade.

"The third key aspect of obtaining a low cost of production is to ensure that the business maintains its comparative advantage over other farm businesses. A business with a low cost of production is more likely to 'win the farming game'."

Snapshot

James is quick to point out that the cost of production for any one year

only gives a snapshot of that business at a particular point in time.

"You need to be very careful in taking too much away from one year's data. To get real value you must complete a minimum of two years and preferably three years before the data starts to have real meaning," said James.

"So it is an ongoing process – once you have two years of data, you can start to compare this data with current market price, expected future market price and the means by which the business can look to improving or lowering the cost of production.

"It may well be that the business is running a very efficient enterprise. All the key indicators in terms of stocking rate/100mm GSR, wool production and lambs per winter grazed ha are all running at a profitable level. To expand on this and increase profits would require significant expenditure on-farm and with the enterprise for a relatively low reward. Such expenditure and focus would leave the business at greater risk to acts of God and other things that will occur."

"Cost of production would isolate that the business problems lay in the overhead cost structure of the business and that the business has a number of means to improve profits. The methods for consideration are cost control in terms of the current cost structure, contract versus machinery ownership, investment to improve labour efficiency or leasing or share farming to spread the existing overhead costs over a greater unit of output."

Remain viable

James said that the potential to increase farm profits in this instance could be greater and potentially involve less investment and less risk than a continued focus on enterprise productivity.

"More profit with less input and less

risk would be a thought that would appeal to most people," he added.

"The farming industry has to deal with declining terms of trade and increasing costs on an annual basis. Anyone farming today has done this well over the past 20, 30 or so years. To remain viable and stay competitive in your industry the challenge is to ensure that you have a business structure and production system that maximises profit. Cost of production is a tool that will enable you to identify areas of strength and weakness and allow you to seek information and advice such that you can remain profitable into the future."

Once you know the areas of strength or weakness, James said you can then identify where to focus management for improvement.

"If the answer lies in production then one can start looking further for information to assist and move forward – for example, Module 10 of *Making More from Sheep* – 'Wear More Lambs', " he explained

"If the answer lies in the overhead costs then looking at the farm system as a whole, the scale of the enterprise and the scale of the individual enterprises will be important.

"Once system changes have been made continued calculation of the cost of production can monitor the progress. With the current turmoil there is probably no better time for producers to look at cost of production."

More information

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