Dairy Enterprise Services
Resources for today's dairy industry

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THE BUSINESS OF DAIRYING

Three overlooked but essential business plan elements

The Cambridge Dictionary defines "business plan" as *a detailed plan describing the future plans of a business*. Have you heard the phrase "the devil is in the details?"

A great number of very talented advisors exists who might offer their opinions regarding important management areas to be included in a comprehensive business plan. If you survey ten such people you would probably see ten lists with different combinations and numbers of suggested categories. I advocate that the following three categories (business risk, succession and milk/feed marketing) are among the most overlooked:

Risk Two dynamics work in tandem to provide a dangerous source of business risk to dairy producers: 1) dairy farms do not tend to retain much cash on their balance sheets, and 2) extreme volatility of milk and feed prices significantly impact a dairy's ability to generate cash over intermittent periods of time to cover their checkbooks (we'll discuss marketing plans later). It is always prudent for a business to manage cash and available lines of credit to ensure that the operation has access to enough working capital to cover cash operating expenses. Within the context of our more recent economic climate, $500 per cow of reserve working capital (either in the form of cash or approved and immediately-available borrowing that is not part of already-planned working capital needs) is not an excessive amount to consider. In order to plan what is needed, an annual operating budget can help shed light on those projected needs. I encourage all of my clients to prepare an annual operating budget for several reasons, not the least of which is that it is a tool that will facilitate an owner's understanding of how cash flows through their operations. The more dairy producers understand what it costs them to produce milk, the more aggressively they can manage those costs.

Succession This function is comprised of two separate and very distinctive elements: asset transfer and managerial succession. Too often neither of these elements is properly planned but managerial succession is the most often neglected. Typically when succession planning is mentioned, we tend to think about estate planning which is a part of the asset transfer process. Succession planning is much more comprehensive and proactive than simple estate planning. How many multi-generational farms can you think of where Mom and Dad are in their 60s or 70s and still control the checkbook and general ledger? Family businesses need to purposely plan how management skills and responsibilities will be most effectively transferred to subsequent generations of owners. (I look forward to sharing more detailed insights to succession planning in the next issue.)

Marketing Market volatility is becoming an almost tiresome subject however, volatility is real and destroys hundreds of dairy operations every year. Many market traders and advisers admit that over the long run, a dairy operation may likely maximize income by *not* hedging and simply ride the cash market and I tend to accept this possibility. However, in order to regain income previously lost in a down market the operation has to live long enough to make it to the next up market. With the extreme trading ranges we have experienced in the commodity sector over the past four to five years, living through the down market to see the next high is becoming increasingly difficult, especially in more highly leveraged businesses. If your balance sheet shows a debt-to-equity ratio of greater than 1.25-to-1, it might be wise to consider developing a consulting relationship with a market advisor and work with them weekly to check when the windows of opportunity are open to lock an appropriate milk income-over-feed margin. It is also interesting to note that several of our industry's seasoned lenders have begun to adjust funding levels with some of their customers based on hedged milk-over-feed-cost margins.

Who We Are

Greg Squires manages DairyES and has consulted in business and financial planning for hundreds of dairy operations in over 30 states. Through this work and a strong background in production management consulting, Greg has cultivated significant relationships with dairy producers and other industry influencers across the U.S.

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If you believe in managing change and are considering steps to improve the productivity and efficiency of your business, DairyES can help you meet your goals. To learn more about DairyES and how we can help lead your business through the process of managing change, please contact us.

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