



Top 10 Keys to Surviving in 2009

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That old saying, “What goes up must come down,” has been proven to be true yet again. After two years of record high milk prices, the inevitable drop has come. The recent fall is the largest drop in comparison to a rolling five-year average since 2000. What makes this situation more dramatic is that this drop in milk price is accompanied by feed costs that are over 70 percent higher than they were during the last downturn in milk prices (2006) and the worst economic crisis in the United States since the Great Depression. So yes, 2009 is going to be a challenging year for dairy producers. But don’t let yourself fixate on this negative outlook. Doing so will rob you of the energy and enthusiasm you will need to tackle the management decisions you will have to make to survive this challenge. Tackle the challenge head on, because those that do survive will be best positioned to capitalize on the opportunities that increasing milk prices will bring. And yes, milk prices will increase again. In fact, the rolling five-year average has been increasing about 18.5 cents per year since 1990. Focusing your efforts on the factors you can control will help minimize losses and ensure that you will survive. Consider these 10 keys to surviving this downturn in milk prices.

1. Assess, Plan and Communicate. The worst thing you can do is **blindly react** to bad economic news without first **assessing** the situation. How bad is it? How bad is it supposed to get? How long do the experts expect it to last? How is this going to impact your business? Are there any possible solutions that might be enacted that could improve things sooner than what is expected? No dairy producer would build new dairy facilities without a set of blueprints. Yet, many operate businesses that generate revenue levels that are equal to or exceed the cost of their facilities without any type of plan. In tight times, it is imperative that you **develop a plan** to provide you with a better understanding of the magnitude of the situation. Don’t bury your head in the sand! Although you may not like the results you see, a monthly cash flow budget will give you an idea of when the business will generate a surplus and when it will generate a deficit. Be realistic! Budgeting for the sake of budgeting is an exercise in futility. Use historical operational cost data to develop your plans. Futures markets, although they are not guaranteed, can provide guidelines for developing income and input cost projections. Once you have a realistic plan, **communicate** it to family members, management, employees, your lender, and key vendors and advisors. They will all appreciate your open approach and will be more likely to work with you through the economic downturn.

2. It is all about CASH FLOW right now; **MANAGE accordingly!** The ability of your business to be profitable over the long run and to thrive when milk prices increase is highly dependent on its ability to cash flow through the downturn. Anything you can do to better manage CASH FLOW over the next year or so should be the focus of your management decisions. Improvements in CASH FLOW can come from multiple sources including: increased revenue, reduced costs, securing additional credit, liquidating assets and/or from reserves. Your plan should address each of these areas. If operations can not provide adequate cash flow, which will be the case in many dairy businesses, will you have access to cash through financing? If not, how will you cover the deficits?

3. Manage information and know your cost of production. Base your decisions on facts, not emotions. Having accurate information on which to base management decisions is critical when managing in crisis mode. A good information management system organizes, reports, and integrates data into factual information, which you can use to make management decisions. ***Evaluate your accounting system.*** If it does not allow you to easily calculate your cost of production and conduct cost center analyses, consider changing to a system that does. Implement a chart of accounts that will provide you with management reports that help pinpoint weaknesses in your production systems. Compare your production costs to those of the top 10-20 percent of profitable dairies. Also, utilize production records, such as DHI records, to evaluate herd performance and keep cows performing at optimal levels. Stay up on of culling decisions to avoid keeping cows around that are costing, not making, you money. ***If you don't measure it you can't manage it.*** There a numerous tools available to help you accomplish this task. Visit our Dairy Alliance website (<http://dairyalliance.psu.edu>) to examine and download them.

4. Analyze Your Cost Centers. On many dairies the primary, and in most cases the only, profit center is milk production. However, all dairies have multiple cost and support centers that flow up through to the profit center. These include the various commodities produced and management activities, such as the dairy herd, replacements, alfalfa and corn silage, as well as milking and feeding operations. Determine if you are raising commodities that are not cost effective. Are operations being run as efficiently as they should? Are you running a milking center that can be operated by one person with multiple operators? Is feeding being done accurately?

5. Implement a management team. Assemble key advisors periodically to help develop strategies to improve CASH FLOW and profitability. Team members may include your veterinarian, nutritionist, agronomist, dairy consultant, extension educator, lender, accountant or financial adviser. By communicating, the team can help monitor trends in key production indicators and help prevent small problems from turning into major catastrophes. Including your lenders will give them a better sense of how the business is performing and increase his/her comfort level with any requests you might need to make in terms of loan servicing. **LENDERS DON'T LIKE SURPRISES!** If you think you will have trouble making loan payments and maintaining sufficient CASH FLOW to effectively run your operation, approach your lender with a plan that may include increasing a line of credit, having loans put on interest only or possibly restructured. Be sure to include how you plan to catch up on your payments when milk prices increase.

6. Control the “controllables.” These include milk production, operational efficiency and marketing. Control what you must to get that next five pounds of milk out of your cows. It is the cheapest milk they will produce, as business overhead and the cows' maintenance costs are already covered. Those five pounds will decrease your cost of production and provide a much needed boost to CASH FLOW. Control mastitis to reduce somatic cell counts and earn milk quality bonuses. Properly balance rations to maximize production while controlling feed costs, and maintain the milk component levels (fat and protein) that influence your milk check. Look for marketing opportunities, but beware, as many producers have gotten burned by getting their feet wet in hedging at the wrong time. Arm yourself with as much information as possible before you act and be prepared to use all the hedging tools available to you if you do decide to hedge.

7. Manage expenses. Realizing that many input costs lie outside of your control, look for areas where you can realize possible *cost savings*. This does not mean blindly cutting costs as many are prone to do in tough times. It means gathering information to see if there are areas where inputs are not providing the returns they did when milk prices were high. Evaluate the cost-to-benefit ratio of each potential purchase, investment or management practice shift. If the marginal cost of a feed additive, or management practice exceeds its marginal return, **DROP IT!** Invest in areas with quick paybacks that contribute additional CASH FLOW immediately through increased revenue or reduced costs. Put off any investment that requires a considerable time-lapse before returns are realized. Although profitability drives cash flow over the long run, in tough times your primary focus must be maintaining CASH FLOW. Manage inventories to minimize carrying charges and control overhead. Examine your labor needs. If you are providing benefits to your employees, ask key employees if they would consider working overtime so that the total number of employees can be reduced, thus increasing your labor overhead costs.

8. Maximize forage quality and feed a balanced ration. High quality forages significantly improve dairy farm profitability and CASH FLOW by reducing the amount of grain that must be fed (reduced feed costs) and providing the foundation for higher production (increased revenue). Since haylage harvest will be here before we know it, make sure your equipment and staff are ready to move when the time hits. Monitor weather to make sure you hit the optimal harvest window, even if it means delaying corn planting. If you utilize a custom operator, you might want to pre-pay to ensure you are on the top of his priority list. (This might not be an option if you suspect your custom operator might have financial issues of their own. The last thing you want to do is pre-pay for services you might never receive.) Manage forage supplies to minimize drastic changes in the forage makeup of the animals' ration. Review variety selection for corn silage to determine if a change is needed to improve the level of DIGESTIBLE nutrients it provides to your cows. Monitor forage quality frequently, and balance rations to ensure that cows get sufficient nutrients to match production levels without overfeeding. Consider the use of alternative storage systems to ensure an adequate supply of fermented feed is available year round. Examine crop input expenses, but be careful not to cut costs to the point that forage quality or quantity will be compromised.

9. Keep cows comfortable. Walk through your facilities. Are cows lying down when not eating? Do they have trouble getting in and out of stalls? Do they have adequate bedding? **NOW IS NOT THE TIME TO CUT BACK ON BEDDING!** Changing to a cheaper source might be an option if it does not adversely impact cow comfort. Do cows wait too long in the holding area? Do they get plenty of fresh air, feed and water? Can they walk without slipping? Can a simple and cheap investment in improved ventilation and cooling keep cows milking better during the summer months? Poor cow comfort levels can lead to poor profitability, through reduced production, poor reproductive performance, higher cull rates and higher feed costs.

10. Invest wisely. You will likely have to put off making any capital investments during this downturn. However, there will be situations where that is not possible. Analyze every investment you make to determine the return it will generate for your business, keeping in mind that CASH FLOW is your major priority right now. Building that new heifer barn might be an excellent idea for improving long term profitability, but certainly not the best decision right now, unless it improves CASH FLOW! However, if you are in a strong enough financial position and have been contemplating expansion, now might be the best time to start your project. Construction costs have dropped, builders are probably looking for business and cow prices are down. If you get it built and filled in time, you could be running at full capacity when the next wave of higher prices hits. As always, PLAN CAREFULLY.

Yes, 2009 is going to present challenges many of you have not yet faced. It is a simple fact that some will not make it through. If you see it looks as though you will be one of those that may not survive, start looking at alternatives before you are forced to. You don't want to farm away your last dollar. I don't know a single person who likes to admit defeat, but I have worked with a number of dairy producers over my 25-plus years in this business who finally had to realize that they had depleted all their options. As stressful as it was for them to go through, I have never had one come back and tell me that getting out was a mistake. *There is life after dairy farming and it can be quite pleasant.* The long hours of farm chores, coupled with the stress of trying to keep a financially distressed business running can take its toll on even the strongest and most determined individuals. If you think you need to explore other options, don't be afraid to ask for help. Your family members, friends, church community and advisors will be there to support your decision. Talk to them! It will not matter what others, outside that circle, might say or think; what ultimately matters is the well-being of you and your family. I could introduce you to more former dairy producers than you might think who would tell you that their quality of life is better today than it was when they were milking cows. I know this first-hand, as my late father decided to get out of the dairy business forty-five years ago and seek employment off the farm. Although he still worked hard and always viewed himself as a dairy farmer, none of us will ever forget the first family vacation we took the summer after we sold the cows.

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