What farmers can expect in next 7 years

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Easing off to 95 per cent production might be preferable to going all-out at 100 per cent, says farm accountant **Pita Alexander**

IT'S a changing world we live in. And it would be right to say agriculture has received its fair share of changes lately and will experience many more in the years ahead.

In my best Nostradamus impersonation a fortnight ago, I raised what I thought would be the key issues farmers were likely to face in the next seven years. We looked at rising costs of production for both dairy and sheep and beef farmers, market competition, volatility and growing water expectations among the many changes they are likely to encounter.

Let's give the crystal bowl another dusting and see what might lie ahead.

1) Probably all businesses are getting more complicated and we increasingly need to think about running them on a level of production that is optimal for ourselves, our business and our profitability. Very often maximum production is not maximum profitability and that can mean trying to get that last 5 per cent margin of gross income exceeded by the last 5 per cent margin of gross costs. At maximum production everybody is under pressure, mistakes are made, people are under stress and machines break down. In many farming businesses optimal production would likely be perhaps 95 per cent of maximum production. Think about this, but remember I am referring to 95 per cent and not 85 per cent optimal production. At 85 per cent you are giving away potential profitability in probably all businesses.

2) If you are going to consistently head for perfection in your business dealings and trying to reach a score of 10 out of 10 all the time, you will be a pain to yourself and everybody around you. Head for excellence which represents eight out of 10. With fine-tuning and time you may get it to nine anyway. Excellence in a business sense is much more important than perfection - don't waste any of the next seven years not grasping this key issue. This period will demonstrate clearly that production is vanity and profit is sanity. Make sure this is not new to you.

3) The present rural/urban gap will unfortunately probably get somewhat wider and deeper. Why? Partly because of dairying and its growth, partly because of water issues, partly because of the constant media space on perceived farming problems and partly because of the elephant in the paddock in the form of Fonterra.

4) Mainstream media spend a lot more space on looking at negative issues involving New Zealand farming and farmers than the many, many positive issues and it is hard to see how the excitement they seem to get from this will reduce over the next seven years. However, if you remove agriculture from the New Zealand economy, you will take out the core of business and many of our journalists' children will need to move overseas to get a comparable job. The research and development constantly going on inside agriculture ably

assisted by Government, Fonterra, Lincoln and Massey universities and the sheep and beef industry are enormous and not nearly enough credit is given in this area. New Zealand has much more respect for this work offshore than onshore which is sad but is life. Many of the New Zealand innovations that get to real fruition end up being bought from overseas and sometimes not with a very big cheque book. It is hard to see this issue changing.

5) We are going to read and hear constantly over the next seven years about income inequality around the world and how unsatisfactory it is. The benchmark for monitoring this is called the Gini coefficient. You will get sick of reading about this because there is nothing you and I can do about it. The Prime Minister presently earns about seven times the average male income, but this is not income inequality and, if anything, is the reverse. Many bankers and heads of business around the world are earning 20 to 30 times their average country wage and this is what you will end up reading ad nauseam. In many cases though this is about very high earners having a very, very sound apprenticeship and absorbing much stress and strain. This writer, like many others, is not helping because we are trying very hard every day to add value to farming and business people's financial affairs mainly to ensure they have good profitability and cashflow. In other words, we are trying to widen the income inequality gap. My advice is let the Government worry about this issue while you focus on your profitability and cashflow.

6) There is no substitute for top advice. Make sure you have people at your shoulder or via your phone that you respect who can add value and can argue with you. Your spouse will be in this group. If you find your key advisers difficult, it could well mean you have good advisers.

7) Timing is everything and the only difference between the top 10 per cent of performers in any industry and the next 10 per cent is in their timing. Looking forward you must really think about your timing. Profits don't manage themselves, but losses do very, very well. Men often procrastinate, but sometimes waiting for the third bounce before you take action has a real place.

8) Farms are the biggest bottomless pits ever invented and will absorb as much cash as you want to throw at it. Think about this because it creates all sorts of problems with succession issues, lack of profitability issues and usually decreasing marginal returns. Anybody can spend money and a man with "iron disease" (loves plant) should never have 100 per cent control over the farm cheque book.

9) With farming getting more complicated and increasing or maintaining profitability almost certainly getting more complicated, we are probably going to see somefarmers looking to invest surplus money off farm as opposed to investing on farm or buying more land.

10) The importance of China is getting more and more crucial to New Zealand agriculture for dairy, sheep, meat and wool. This is all workable but when we depend more and more on one market, the suppliers, that is New Zealand farmers, and their key institutions and co-operatives must build their financial reserves to cope almost certainly with major hiccups at some point. Farmers feel they have major net asset reserves, but that only applies when their banks are happy and positive and they have in anything but very sound years quite

weak financial reserves in terms of income. This could well turn out to be a crucial issue for farmers. They need to build their financial reserves and build them quietly but ruthlessly. How much? I would say don't stop building them until you have 20 per cent of your gross farm income in financial reserves.

11) If a capital gains tax of some kind comes to pass, it will probably only apply in the main when you sell a key financial asset to another party (with that party including family). Have a look at your present ownership and operating structure. It would probably help if you had a setup that could remain in its present form for some time before any sale or transfer.

12) Anybody can package "Yes", but how you package "No" requires a lot more skill, patience and personality. Make sure you can package "No" well, whether it is with employees, business parties, family or spouse. That is a major business attribute that will provide major returns if you can get it right.

13) Right now dairy farmers should look hard at making voluntary income tax payments for the year as soon as possible. Underpayments of provisional tax for whatever reason will potentially mean the Inland Revenue Department will impose significant "use of money interest" charges. This area needs action now.

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