Over the past several months we have discussed many ways that producers can lower the input cost per cow in their operation. Suggestions have ranged from increasing calf crop percentage to being aware of the cow's body condition score year round to controlling weeds in your pastures. This week we will discuss a method that is perhaps not as widely implemented as the many suggestions we have previously offered. We will look at the financial impact that fixed costs have on an operation, identify the most common types of fixed costs, and offer suggestions of methods to decrease these costs in your operation.

In a recent lecture given by economist Stan Bevers, he stated that 45-50% of the total costs in a cow-calf operation can be attributed to fixed costs. Certain vehicles, equipment, and other items are necessary regardless of herd size. These items are considered fixed costs. In Mr. Bever's words, "Fixed cost doesn't care whether you've got 400 cows, 200 cows, 60 cows, or 2 cows. It's going to stay the same." Mr. Bevers also explained that labor/management, and depreciation (both fixed costs) are the two most expensive costs incurred by the average rancher. This information reveals the importance in keeping fixed costs to a minimum in order to maximize profitability. In fact, Mr. Bevers performed a study on 60 herds of cattle ranging in size from 47 cattle to 3,000 cattle. He then grouped the herds according to the amount of net income they made per year. The Thrivers were the producers that had a net income up to $150 per female. The Survivors group was comprised of producers that either broke even, or had a net loss up to $50 per female. Lastly, the Nose-Divers were the producers that experienced a net loss up to $250 per female per year. (See Figure 1 below)

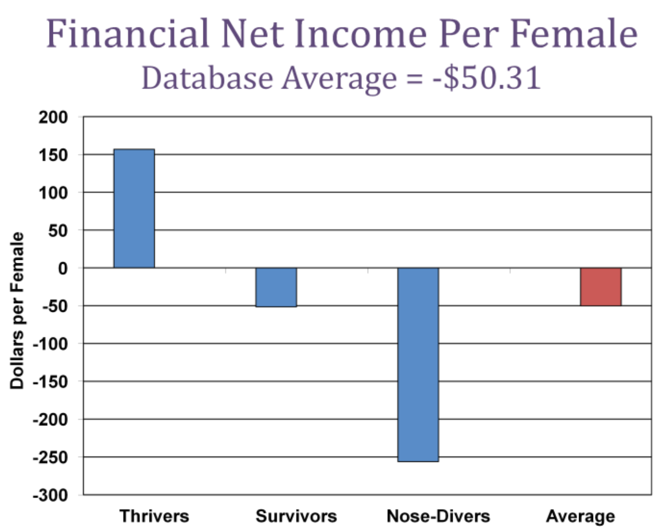

Figure 1

As you can see in Figure 2 below, herd size and net income were not correlated at all.

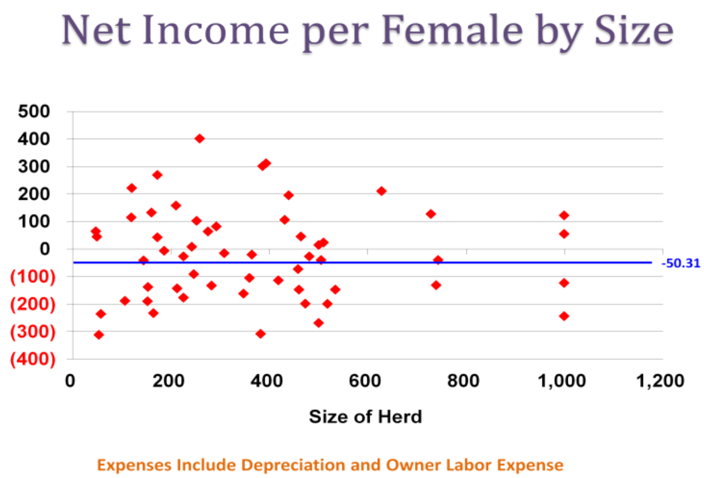

Figure 2

Mr. Bevers closely evaluated these three groups and discovered a significant difference that set the Thrivers apart from the less profitable groups. The Thrivers top three expenses were feed purchased, labor/management, and depreciation respectively. The other groups top expenses were labor/management, depreciation, and feed expenses. That is, the Thrivers (the profitable producers) found a way to keep their fixed costs low.

Many producers believe that a simple way to reduce input costs is to sell some cows. This is not always a cost efficient management decision. If you decrease herd size in effort to decrease input costs, a fixed cost should be decreased as well. For example, sell some cows, but also sell the piece of equipment that you are paying depreciation on, and can do without. Due to the huge impact that depreciation and other fixed costs have on the profitability of an operation, it is important to keep these costs as low as possible. Often, this may require some difficult decision making on your part. Next time you are considering purchasing a piece of equipment or any other item for your operation first stop and ask yourself “Is the __________ that I am considering purchasing going to improve my cow-calf operation reproduction and/or production efficiency?”

Fixed costs are an important piece of the puzzle in determining whether or not your operation is profitable. For more information on decreasing fixed costs, or to learn more about Mr. Bevers’ lecture, please contact us.