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ECONOMICS COMMENTATOR

South Dakota State University

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OBSERVATIONS FROM EXTENSION MARKETING/FARM MANAGEMENT EDUCATORS

Four Extension Educators specialize in working with local producers and agri-businesses on marketing and farm management issues. They also work closely with Extension Specialists in the Department of Economics. For this *Commentator*, we asked them to highlight economic observations or concerns they have encountered in their field education unit (FEU) that may be relevant for our readers to consider. Contact information for each educator has been provided if you would like to discuss these or other issues.

Production Considerations

Heather Gessner
McCook County, North 1 FEU, ph. 605-425-2242

In McCook County producer concerns are pretty much par for the course. They have been gearing up for calving and planting seasons. Questions about the weather, insects, weeds and BSE remain top coffee shop topics, as well as what the crop markets will be like at harvest.

At this time, producers are wondering if they should consider locking in corn prices in order to feed cattle this fall or if they should plan on selling their calves at weaning and the corn at harvest. Row crop producers have been looking into different pricing strategies to lock in a floor price for part of their anticipated production. They have been talking to their crop insurance agents to determine how much they can forward contract under their insurance policies. The inverted markets have them wondering about how high, or low this market will go.

On the crop planting side, there is not as much talk this spring as there was last fall about rotating a small grain crop back into the rotation and rotating some bean acres out. Their reasons for the switch were that the additional cost of spraying for soybean aphids and bean leaf beetles makes the profit spread between beans and wheat a lot narrower.

Producers are also looking towards more normal crop production this year. Bin sales have been steady to higher around the area. With high price expectations and hope for large crops, sales are up despite the rise in the cost of steel. Steel prices have increased sharply and manufacturing companies have started to ration out the steel they have on hand to their retail customers.

Producers at the recent *Carcass to Compost* program asked questions from specialist in the areas of building design, biosecurity, permitting and startup and maintaining a compost pile. Economic considerations of rendering service pick-up costs and availability were also part of the discussion. Due to increasing costs, producers were looking for an alternative method of carcass disposal. Those in attendance were shown different building alternatives and were also introduced to a "winrow method" that would not require additional cash output for buildings. Another key issue was disease containment in day-to-day death loss and in the event of an emergency. Producers were informed that some diseases like BSE and anthrax would not be killed through the composting process, but other bacterial and viral diseases would be.

Water Quality

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Western South Dakota is again faced with the prospect of drought. In some parts of the area, producers are facing the third to fifth year of below normal precipitation. Producers are concerned with a lack of surface water and conditions of their springs and wells due to the lack of moisture. The quality of water is just as important as quantity of water. Dr. Trey Patterson and other SDSU researchers have been studying the effects of water containing high levels of total dissolved solids (TDS) and sulfates. They determined that surface water containing high levels of TDS and sulfates adversely affect cattle performance and health 1) by reduced water and feed intake; 2) by

toxic levels of sulfur ingestion; and 3) by induced trace mineral deficiencies. Extension Educators have electro-conductivity meters that can accurately test for TDS and sulfates for livestock consumption. Producers are searching for alternatives to poor quality water. Three possible alternatives to consider are: 1) hauling water to livestock; 2) water filtration systems; and 3) installing wells and pipeline systems.

Producers who have a good quality feed source but poor quality water might choose to haul water to livestock. A producer might have a supply of quality water at another area or have a flowing river or irrigation district to use as a steady water source. Some may have to purchase water through a rural water system or city water source. The down side to hauling water is the miles of travel and time it takes. Some producers have had to invest in a tank and drive over 100 miles a day to provide water for their livestock. To accurately determine the cost of this alternative you must consider the water fee, gas prices and vehicle maintenance and the producer's operational cost of hauling water.

For the producer who has an ample supply of water, but with high levels of TDS, sulfates or other minerals, a water filtration system may be an alternative. A filtration system for livestock can produce from 100 to 10,000 gallons a day. The average cow consumes around 40 gallons per day, depending on the temperature. A filtration system would need to produce over 4000 gallons a day to sustain 100 head of cows. A reverse-osmosis filtration system would be needed to treat water for TDS and sulfates, which would cost around \$11,000 to install.

For the producer who has a low quantity of poor water, digging a new well and installing a pipeline system is something to consider. With this option costs can be very high and implementation can be time consuming. Water from a new well could also contain high levels of TDS and sulfates, something that cannot be determined until it is dug. A pipeline system needs to be thought out carefully to determine where tanks should be placed. The costs associated with digging a well and installing a pipeline system vary, but could cost \$100,000 for a 3000 ft well; \$1-\$3 a foot depending on pipe size and type plus \$500-\$700 for each water tank, and if a pump is needed, electricity or generator costs.

The benefit to good quality water is recovered in improved animal performance. According to Dr. Patterson's study, cows on high sulfate water lost 36 pounds whereas those on the low sulfate water gained 10 pounds. Research is ongoing to determine the critical salt levels in water where calf weaning weights and cow reproduction are affected.

To determine which choice is right, producers must consider: cost, amount of use, feasibility of water, and the benefits from providing quality water to their livestock.

Traveling Regulations

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New federal trucking regulations will likely impact the average farm in South Dakota that uses trucks to move agricultural commodities or farm supplies. It will significantly impact farms that are in remote locations. For producers, such as those here in Jerauld County, these changes make it more difficult to access markets more than 114 miles away by truck.

In 1939, the motor carrier industry implemented hours-of-service (HOS) regulations for truck drivers. Over the course of time, roads and vehicles have been dramatically improved to allow longer distances, greater access, and higher safety standards. Over the past several years, the Federal Motor Carrier Safety Administration (FMCSA) has considered changing these regulations.

Starting in 1995, with a mandate from Congress, the FMCSA began a rulemaking procedure to increase alertness and reduce fatigue in drivers. After extensive hearings and reviewing over 53,000 individual comments submitted during the process, the FMCSA issued the first major change in the HOS regulations since their initial implementation.

Starting July 1st, 2004, South Dakota will adopt the new federal guidelines stating that truckers can drive up to 11 on-duty driving hours; however, this must be followed by 10 consecutive hours of rest time.

Agriculture does have an exemption to this rule. During planting and harvest seasons, drivers hauling agricultural commodities or farm supplies for agricultural transportation and marketing operations have unlimited hours as long as they stay within a 100 mile radius by air, or 114 mile radius of driving from the home farm or agricultural business center. Planting and harvest seasons in South Dakota are classified by the State as March 1st through December 31st.

This is where people in some parts of the state will struggle. Processor or elevator locations such as Volga and Sioux Falls are both over 114 miles away

for some operations in Jerauld County. Therefore, they will need to submit to the 11 hour rule, even during planting and harvest seasons. All of these HOS regulations apply to trucks with four axles or more, and with a gross weight of 26,000 lbs or more for intrastate travel. Trucks not meeting this standard are not required to follow the HOS guidelines. FMCSA had plans to eliminate this exemption, but influence from the USDA has kept it in place when the new changes come.

Some other important changes include: (1) Driving is permitted seven days a week for up to a total of 60 hours. (2) Alternatively, cumulative work for eight days is permitted up to 70 hours. (3) No nighttime or weekend restrictions apply. (4) No in-cabin electronic monitors are required for compliance due to technological and privacy concerns. (5) No changes in team-driving requirements apply. (6) On-duty status can be reset after 34 hours of continuous off-duty time.

With an estimated 89% of all agricultural products currently being transported by truck, this may have a significant impact on agriculture. For further information, go to <http://www.fmcsa.dot.gov/>.

These new regulations could have serious implications for producers and others transporting agricultural goods. Producers unable to travel under the HOS regulations will be more likely to take a price at local elevators. This may put the producers at a disadvantage by reducing their potential markets. Elevators will be less likely to truck grains when trains are backed up—also a big problem locally. Elevators may pay less for grain due to larger on-hand quantities. Even though grain prices are higher, we could see a wider basis at harvest.

Farm Financial Management

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Land Rental Arrangements

In recent weeks, a number of producers and landowners have been updating their written contracts for the coming crop planting season. I have used two sources of information in answering related questions for producers: *South Dakota Farmland Market Trends 1991-2003* – SDSU Department of Economics and *South Dakota 2003 County Level Land Rents and Values* – NASS.

Most questions related to what was happening with negotiated prices during the winter of 2003-2004. Some people were looking at one year contracts while others were looking at longer term contracts.

Factors driving changes in rental rates, from opinions gathered from producer and owner interviews, are the new farm program's impact on farm income and increasing land values due to sales (which increase taxes). Most retired land owners have land rents as the major source of income and are concerned when their expenses (i.e., taxes) go up. According to the *South Dakota Farmland Market Trends 1991-2003*, the most recent annual change in ag land values was 9.7% compared to the ten year average annual rate of 6%. From 1996 to 2003, cropland values increased 7.2% annually while cash rental rates for the same period grew by 6% annually.

Over the last couple of years of *Pricing for Profit* programs in northeastern South Dakota, we have found that as farm income goes up, landowners are very adept at getting their share of that income. As the average farmer age continues to increase across South Dakota, crop production is concentrating in fewer hands. As young people return to the farm, it is becoming increasingly harder to find land at a low enough cash rent price to get started. Cash rent auction prices are increasingly higher and producers are expecting increases in cropland cash rental rates in northeastern South Dakota to exceed 10% and may be close to 15%. Most county assessors in northeastern South Dakota reported increasing farm values of around 9% for 2004 based on 2003 sales.

One concern with using past history and land rent averages is that it does not tell producers what most people are charging or paying for land rent. The numbers being reported are surveys filled out by producers in most cases. Interviews that I have had with landowners and renters over the years suggest that the lower cash rents are not being reported because they may be between family members, relatives, etc. This in turn increases the reported average cash rent above what may be the true value.

SPA Versus FINPACK Cow/Calf Analysis

Over the last year, I have had the opportunity to work with cow/calf producers in northeast and east central South Dakota or SPA and FINPACK. SPA is the National Cattlemen's Beef Association's Standardized Performance Analysis and is based on the Farm Financial Standards. SPA uses cost basis values for balance sheet inputs associated with the cow/calf enterprise.

SPA provides two methodologies for analysis; they value assets differently, and they are used for different

purposes. The first is a financial analysis, which values assets at their cost or depreciated value (book value). The second is an economic analysis, which values assets at their market value. According to *Agricultural Financial Reporting and Analysis*, an appropriate use of a financial analysis is to evaluate managerial efficiency and an appropriate use of an economic analysis is to evaluate an entry or exit strategy for a business. When using an economic analysis, deferred taxes must be included. To mix the methodologies is inappropriate and confusing.

SPA is designed to calculate the unit cost of production. Expenses used in SPA are only those associated with the cow/calf enterprise. Most producers in eastern South Dakota have to figure equipment and other expenses on an allocation basis with other farm enterprises such as back grounding calves and the crop operation. Looking at different alternatives is cumbersome and SPA is not really designed for that purpose. It also has trouble fitting purebred beef operations, but can be adapted.

This winter I started working with beef producers using 2003 FINPACK, agricultural software developed by the University of Minnesota that helps evaluate the farm financial position, explore alternatives, and make business decisions. FINPACK's balance sheets differ from SPA by allowing assets to be valued at cost, market, or both and by having two columns for them if both are selected. FINAN

takes an in-depth look at the whole farm's cash financial strengths and weakness while the Enterprise analysis portion looks at each enterprise in the operation. Both SPA and FINAN use an accrual income statement. Cow/calf producers who have completed FINAN Enterprise analysis find it easier to complete the financial section of SPA. Balance sheet inventory adjustments are handled similarly in SPA and FINAN with information based on changes from beginning balance sheet and ending balance sheet on a yearly basis. SPA production inventory adjustments are based on the start of the breeding season the previous year working until weaning of the calves. Producers sometimes find it confusing to work with two time periods, one working with balance sheets and income statements, and the other working with the breeding season through weaning.

Once the strengths and weaknesses of each program are known, either can be used to evaluate profitability of the cow/calf operation.

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