VALACTA – Dairy Production Centre of Expertise

Falling prices, rising quotas: What are the prospects for my farm?

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Since January 2015, Quebec dairy farms have seen their right to produce increase by a little over 15 per cent, in addition to the many extra production days allowed and the usual fall milk incentives. Unfortunately, the average price for a hectolitre of standard composition milk decreased by seven per cent during that same period. Producers experienced the short-term financial pressures and human stress stemming from that situation. Now that the initial shock has passed, however, it is time to gauge the impact of this new reality and figure out how to make the best of it, based on each specific situation.

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Take advantage of the right to produce to compensate for lower prices

Let's take a look at the example of Bright Future Farm, a fictional 60-cow operation with a 60-kg quota in January 2015. Table 1 shows that in 2014, with a 60 per cent spending rate, the farm had a maximum repayment capacity of nearly $100, 000.

The second column of results shows that this number will drop to $68, 600 in 2017, if the farm is unable to produce the additional quota made available in the last two years.

Finally, the last column illustrates that the quota increases make it possible to raise the farm's total income in spite of lower prices while maintaining a repayment capacity similar to that in 2014. Note that operating costs and wages have been increased accordingly to take into account the higher production volume.

And if the barn is already full?

Farms in a good financial position who had chosen to set aside their building upgrade plans could possibly dust them off in 2017. For producers who prefer not to go that route or who require a few more years before doing so, there are other possibilities to consider. One of many options would be to custom raise your heifers to free up space in your barn for lactating cows. Based on our calculations, the margin generated would allow you to recover the costs of the barn updates within a few years.

Invest to produce more

Whether short of space or not, it may be necessary to invest in a building or in equipment to be able to produce the additional milk. An investment ranging from $50,000 to $100,000 for minor changes that enable the farm to produce additional quota will be recouped within five years. This is a good alternative for those who are not ready to commit to a long-term project, either because they are unsure about who will take over the farm or because they are in a tight financial situation. On the other hand, a project involving a new dairy facility worth more than a million dollars is an option reserved for those who are in a solid financial position with clearly defined long-term goals, and one that is based on substantial productivity gains.

Sell surplus quota

Producers who are unable or unwilling to expand their operations to produce all this milk might very well consider selling their surplus quota. Forget the idea that this marks the beginning of the end; it is not a matter of selling your base quota but simply the portion of the extra quota that you will be unable to produce in the coming years. There is no point in holding on to something that offers no return. The equity recouped from the sale could be used to repay debts and make ends meet at the end of the month.

This approach requires careful preparation, however. You need to plan judiciously to ensure a sufficient production margin and evaluate the fiscal impact of the quota sale with your accountant.

In conclusion

How will things change in the future? Will we be able to count on an upturn in prices or a steady increase in consumption? Making predictions of this sort is risky business. Without a crystal ball, the best way to ensure the sustainable development and prosperity of our dairy farms is to continue to work towards reducing our production costs.

Table 1. Financial impact of the decrease in price and increased quota on Bright Future Farm

	2014 results	2017 budget, production quota for January 2015*	2017 budget, production quota for January 2017**
Gross revenues (milk + animals)	$471,200	$439,800	$508,000
Operational costs	$282,700	$282,600	$316,500***
Wages and withdrawals	$88,600	$88,600	$93,100***
Maximum repayment capacity	$99,900	$68,600	$98,400

*volume prior to quota increases in 2015 and 2016; milk price: average price for 2016
**volume after quota increases in 2015 and 2016; milk price: average price for 2016
***marginal cost adjustment

[1] Spending rate: operating costs ÷ gross revenues
This example shows that farms that can produce 100 per cent of their quota increase are able to regain solid financial footing, regardless of the reduction in the price per hectolitre.