Farm Financial Viability “How Big is Big Enough?”

Is the size of the operation important? Well the answer is simple, “It depends”. It depends on several interrelated factors. Cash farm profits need to be large enough to pay for both the family living needs as well as the principal portion of the debt obligations therefore the three factors that determine “How Big is Big Enough?” are: Type of farming/ranching operation, the amount of farm contribution needed to provide adequate income to pay for family living needs and the size of the principal payment obligations of farm debt service.

1. What type of farming operation do you have? Is your operation a traditional “mid-west commodity” type of farm in which you raise genetically engineered corn and soybeans? Is it a fertilize, plant, spray and harvest, crop operation or a large confinement factory style livestock operation that is characterized as a high capital investment, high sales volume, low profit margin operation. Or is it a specialized farm that produces products for a specific high profit market such as an organic farm or a locally grown niche market such as CSA or a farmer’s market? Production of this type is characterized as a lower capital investment, low sales volume, higher labor, and high profit margin operation.

2. What are your expectations about family living? Do you need $10,000/year to cover your family living costs? How about $30,000 or $50,000 or $150,000? If you need $50,000/year to pay for your family living costs and your farming operation is operating at a 10% cash profit margin, you need to generate annual sales of $500,000/yr to create $50,000 of profit to cover your family living costs. If your family living is supplemented by non-farm income of let’s say $20,000 then you only need $30,000 from the farm to create enough income for your family living. $30,000 would be generated by annual sales $300,000 at a 10% cash profit margin.

3. What are your debt obligations and precisely how much principal is due each year? If you need an additional $10,000 per year to pay your principal obligations on a loan you would need to generate an additional sales volume of $100,000 at a cash profit margin of 10%.

Traditional “Commodity” type operations tend to have cash profit margins that average from 10% to 20%. Specialty operations usually have a much higher cash profit margin. It is not uncommon to see organic operations that can reach a cash profit margin of 50% or higher. Thus the size of the operation can be greatly reduced if the type of production is a higher value commodity. The size of the business is also influenced by the amount of debt that needs to be repaid. If debt repayment can be structured so the obligation to pay principal is stretched out for a long period of time with no penalty for early repayment the need for a larger amount of profit can be reduced.

What game do you want to play? There are many considerations but ultimately the choice is yours.