How Can You Reduce the Impact of the Cattle Cycle?

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The Beef Cattle Industry has a long history as a cyclic industry (Figure 1). This is a result of the functioning of the classic economic theory of "supply and demand." The supply, or number of cattle, fluctuates with the price, or profitability (demand) of the industry. When numbers are down, the price (demand) goes up and it becomes profitable to raise cattle; so cattlemen save more heifers to add to their herds and more herds are created. In a few years more cattle are available for sale than are needed at profitable prices, so the price drops and it becomes unprofitable to raise cattle—until the supply becomes smaller (Figure 2). This explanation is oversimplified because other factors, like feed supply and economic conditions, influence prices and profits, Since records have been kept and reported, the cattle cycle has been functioning on a 10-year average with amazing consistency. There has been some variation in the length of the phases and the length of the cycle. Knowing the pattern, how do cattlemen cope?

In my travels and visits with cattlemen around the state I have found that there is a wide variety of approaches to this problem, which can generally be summarized by ***three basic methods***: (1) invest part of the profits each year in liquid investments (such as certificates of deposit, money market accounts, mutual funds, etc.) for use as operating capital in years when there are no profits; (2) diversify into other enterprises like citrus, timber, vegetables, ornamentals, or sod; (3) expand herd numbers during good times (through additional fertilizer, improved pastures, keeping more heifers, etc.), and reduce numbers to maintain cash flow during bad. Few ranchers follow any one of these methods precisely; most use some combination that fits their particular situation and resources.

The cattlemen most successful with ***Method 1*** are generally good businessmen who are comfortable dealing with financial institutions and products. They also have the discipline to allocate a portion of any profits to the "rainy year fund."

Method 2 requires suitable resources to profitably produce the commodity with which you diversify, and still have a viable beef production unit. Diversification simply means you don't have all income coming from one commodity and you're hoping they won't *all* have an unprofitable year at the same time. The key to successful diversification is having adequate resources and knowledge to be profitable in all commodities you are producing.

With ***Method 3***, ranchers are able to concentrate on a product that they believe they have the necessary resources and management skills to successfully produce. In good (profitable) years, they invest in equipment with a long payback (like tractors, trucks, corrals, etc.), which helps reduce taxes, as well as reducing operating expenses by lowering repair costs. They also fertilize and manage pastures to improve productivity in order to increase the number of cows in the herd. In poor (unprofitable) years ranchers sell unprofitable cows, which brings in more dollars, reduces pressure on pastures by allowing less fertilizer use, and (at times) reduces taxes through capital gains provisions. If feed cost relative to the value of heifer calves is right, they keep cheap heifer calves and market the higher-value bred heifers and cows. Another alternative is to keep light, late calves and cutbacks that are low-value, sell some cows to make room to grow some winter feed, and then sell the calves in the spring or summer when they weigh more and the market is stronger.

The key to success is being able to economically winter the calves and put some growth and low-cost gain on them. The successful manager tries to effectively use the resources available in order to make the ranch profitable and survive the low markets. Keeping production costs low makes this process easier (Figure 3). Many times this requires being flexible and adapting to new situations by changing traditional management practices.

The important step in dealing with a cyclic business is to recognize that it will have periods of profitability along with periods when it will be unprofitable, and to develop a long-range plan emphasizing resource development and improvement during good years, to allow minimizing expenditures during unprofitable years.

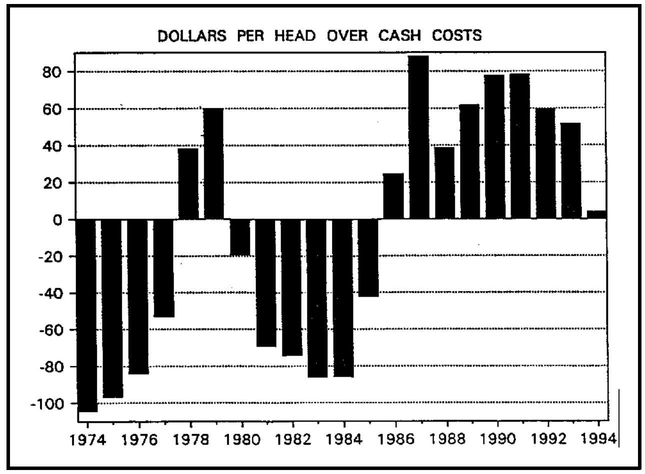

Figure 2. Estimated average cow–calf returns.

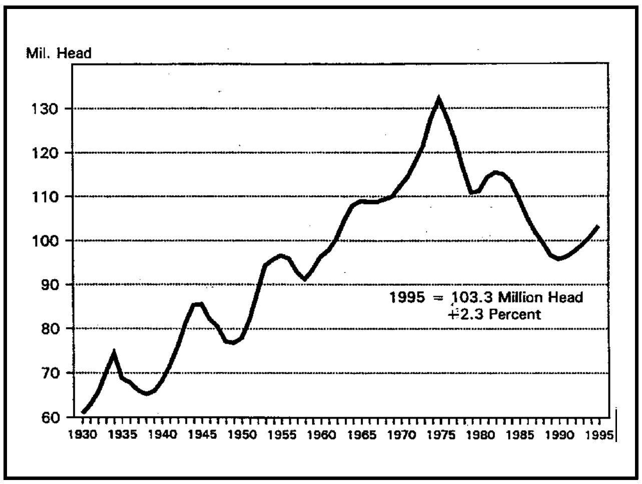

Figure 1. January 1 total cattle inventory, 50 states.

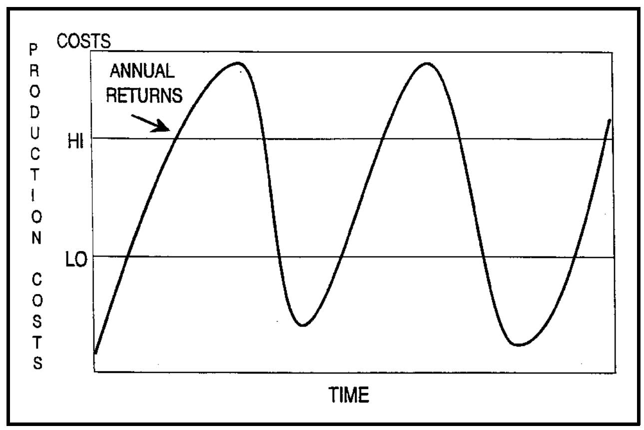

Figure 3. Production costs versus returns.