ALUMNI NEWS

Realize *your* vision AME AGRI-FOOD MANAGEMENT EXCELLENCE

SPRING 2018

Join AME and CTEAM/CFAME Alumni *at the Calgary Stampede!*

Calgary Stampede

This year we are hosting an AME Alumni event in Calgary July 10 – 12th.

We will be begin with tours on the 10th, starting the day off at Big Rock Brewery with a tour and beer tasting. The next stop is the Glengary Bison Ranch, and we'll finish off the day taking a tour (and of course more tasting!) at Hilton Ventures and Origin Malting and Brewing Co., a craft brewery started by Sterling Hilton, AB Farmer and Chair of Farm Management Canada. Sterling's grain farm, Hilton Ventures produces the malt barley for the craft brewery. It will be a great day to learn about different business strategies and challenges.

On Wednesday, July 11th, Merle Good from GRS Consulting Inc. will talk about retiring into your child's farm company – would you rather be a creditor or a shareholder in your farming child's company? Larry Martin will be discussing the AME/ BDO project and will summarize the results to date of the project, illustrate how they can be used in management, and update next steps. Tom Droog, founder of Spitz Sunflower Seeds which grew to $32,000,000 in annual sales, will offer valuable advice and experience on managing growth, staying on top of your company's finances, branding, and his experience in the export market. Lawrence Rowley will finish the day sharing with you plans for AME Alumni AgriTechica 2019 in Germany.

The first 25 people who register for this program will receive an invitation to the International Agriculture Reception held the evening of July 11th on the Stampede grounds.

This distinguished event is held to bring members from the world's agricultural community together to share ideas, to facilitate business opportunities and to foster friendship and cultural understanding.

As an optional add-on, for those of you who want to join us for a day at the Stampede, we have tickets available for the Rodeo, Chuckwagon races and Grandstand Show for Thursday, July 12th. You can customize how you want to spend your time at the Stampede.

The hotel is perfectly located within walking distance to the Stampede grounds and other festivities and included in the event package price at terrific rates.

For detailed information and to register, visit: ***www.agrifoodtraining.com/for-ame-alumniofcteamandcfame***

INSIDE THIS ISSUE:

CPTPP and Canadian Agri-Food

By Larry Martin

Canada finally signed, along with its 10 cohorts, the renamed CPTPP (Comprehensive and Progressive Trans-Pacific Partnership) in March. It was renamed because the wise leader of the country who had the most impact in its negotiations decided to pull out. So, it's only 11 nations instead of the original 12.

So, what are the implications for Canada's agri-food sector resulting from this treaty?

Most of it is about gaining market access – i.e. removing barriers to trade. From a Canadian export perspective, the prize in the group was the highly protected Japanese market, with producer subsidy equivalents of around 50%, indicating one of the highest levels of agricultural protection and subsidization in the world. Malaysia, Singapore and, especially, Vietnam are also highly protected.

What Canadian Agri-Food Gained

CPTPP offers considerable opportunity for market access. Here are some overall and then specific changes to trade policy that come out of the treaty.

Japan will eliminate tariffs on 32 percent of ag and food tariff lines to other TPP members immediately upon entry into force (as soon as it's ratified and CPTPP is actually initiated).

- 9 percent of tariff lines will be provided preferential tariff treatment through permanent quotas and country-specific quotas for Canada.
- Remaining tariff lines will have tariff elimination or reductions over up to 20 years.

Vietnam will eliminate tariffs on 31 percent of its tariff lines

- 67 percent of tariff lines will become duty-free within 15 years,
- Remainder being provided preferential treatment through other means (e.g. tariff elimination only on in-quota tariff lines).

Malaysia will eliminate tariffs on nearly 92 percent of its tariff lines.

- 7 percent of tariff lines will become duty-free within 15 years
- Remainder being provided preferential treatment through permanent TRQs.

Here are some specific examples of what those changes mean:

Pork

- In Japan, tariffs of up to 20 percent on pork products, including sausages, which are subject to the gate price system will be eliminated within 10 years.
- Tariffs of up to 27 percent in Vietnam on fresh/chilled and frozen pork will be eliminated within nine years.

Beef

- In Japan, tariffs of 38.5 percent on fresh/chilled and frozen beef, as well as tariffs of 50 percent on certain offal will be reduced to 9 percent within 15 years.
- In Vietnam, tariffs of up to 31 percent on fresh/chilled and frozen beef will be eliminated within two years, and tariffs of up to 34 percent on all other beef products will be eliminated within seven years.

Wheat and Barley

- In Japan, Canada will have Canada-specific quota for food wheat starting at 40,000 tonnes, then to 53,000 tonnes within six years. Mark-ups (tariffs) within this country-specific quota will be reduced by 45 or 50 percent.
- Canada will have access to a CPTPP-wide quota for food barley which starts at 25,000 tonnes and grows to 65,000 tonnes within eight years. Mark-ups applied to the price of food barley by Japan will be reduced by 45 percent within eight years – from $150/tonne to $85.

Processed Food and Beverages

- Canadian exports of processed food products and non-alcoholic beverages face high tariffs from CPTPP countries such as Japan and Vietnam.
- For example, Vietnamese tariffs for frozen French fries are 24 percent.
- The CPTPP will eliminate or reduce many of the existing tariffs or create tariff rate quotas on processed foods and non-alcoholic beverages, including maple syrup, baked goods, processed grain and pulse products, and sugar and chocolate confectionery.

All the modelling work that has been done on the effects of TPP and CPTPP show that Canada will be a net beneficiary to the tune of around $3.4 billion. The largest benefits are to the agricultural sector, especially pork, beef, grain and oilseed industries including the processing components. My observation is that the actual gains from trade agreements are larger than modeling results suggest because of the structural changes that occur. For example, if the very substantial reduction of Japan's tariff on canola oil is enough to stimulate new investment in efficient processing facilities, the impacts would be larger than the models suggest because the models don't include the structural change.

The same argument can be made for pork, beef and grain processing facilities.

It is important to also understand that Canadian agri-food stands to have additional gains because of the fact that the U.S. is not included. So, for example that reduction in Japanese tariffs on wheat from $150/T to $85 applies to Canada and Australia, but not the U.S. This gives non-U.S. countries an advantage, as does the growing reputation of the U.S. as a disturber in trade.

Similarly, there are gains in the agreement for Canada relative to other TPP members: e.g. Australia has advantages in market access in Japan because of a bi-lateral agreement between those two countries. The advantages will be eliminated or reduced by CPTPP.

What Canada's Dairy and Poultry Industries Lost

Most of Canada's agri-food sector has little trade protection, so Canada's major concessions on market access were for the dairy and poultry. In these industries, Canada has "Tariff Rate Quotas" (TRQ's) as well as well as quite high tariffs.

In Canada's case TRQ's are a percentage of domestic consumption that can be imported tariff free: the tariffs are applied on imports above the TRQ level. The amount of TRQ varies by industry, but the minimum is five percent of domestic consumption. So, we'll use 5% to illustrate how it works.

Let's use butter as an example. Following from the explanation above, assume that Canada has allocated 5% of domestic consumption to its TRQ for butter. That quantity would come in with no tariff. Once the TRQ's are filled, the next kg of butter has a 300% tariff. So, the imports are unprotected within the quota, but highly protected thereafter.

While the supply managed industries resisted giving any concessions, it is apparent that they have expressed less concern with expanded TRQ's than dropping the tariffs: e.g. Canada gave several thousand tonnes of cheese quota in the European trade agreement, and the rumours are that additional TRQ is what is being negotiated in the NAFTA negotiations.

In CPTPP, Canada will give 3.25% more TRQ for dairy products and 2.0% each for chicken, turkey and eggs. New Zealand and Australia will likely benefit from the dairy TRQ's and Chile for poultry, at least for turkey.

This trend toward increasing Canada's imports through more and more free imports looks like the beginning of a substantial self-inflicted wound, especially if even more is given up in the NAFTA negotiations. Doing this rather than negotiating tariffs seems to be short sighted: as long as foreign product can be priced below Canadian product, we simply hand over that share of our domestic market to the foreign supplier. Negotiating tariffs would at least give the Canadian industry a chance to compete in its own markets.

It would appear that Canadian tariffs can decline markedly without giving up much protection. An example using butter will illustrate. A major part of Canada's milk prices are based on fixed support prices for butter and skim milk powder. Currently, Canada's support price for butter is C$8.00/kg. The whole concept of the policy is to keep imports out by making their landed cost higher than the support price. The landed cost is value in the foreign market plus transportation costs and tariffs.

According to the USDA, the average wholesale price of butter in the U.S. the week of March 24, 2018 was just over U$2.20/lb. This is approximately U$4.85 per kg. Converting it to Canadian at a $.78 loon, gives a U.S. price in Canadian funds of C$6.22. So, ignoring transportation costs, U.S. butter with a TRQ can be sold in Canada for a very healthy profit of $1.78 ($8.00 - $6.22).

Now let's calculate the landed price in Canada (again ignoring transportation costs) for U.S. butter with the nearly 300% tariff. 300% of C$6.22 is C$18.66. Adding the tariff to the cost of $6.22 gives a landed price of $24.88. In other words, at least in the current situation of relatively low dairy prices in the U.S., Canada's tariff is far higher than what would be needed to keep imported butter out of the Canadian market. This is rather like using an artillery barrage to kill a fly when a flyswatter would suffice: in this example, the fly swatter would be a minimum $1.78.

Despite this, Canada continues to negotiate more and more free access to our market, leaving a declining percentage for domestic producers.

Summary and Implications

Canada's entry into the CPTPP gives many of our agri-food industries much better access to higher priced markets in Asia where concentrated populations have diminishing amounts of land and water available to produce food, while Canada has the third largest endowment of arable land per capita and likely the largest endowment of fresh water.

As indicated above, the decision to give up additional market access to dairy and poultry does bring into question whether doing so as additional tariff rate quota instead of reducing tariffs is the best approach for those industries.

The agreement also improves Canada's access relative to other major exporters such as Australia and New Zealand, and particularly the U.S. since the U.S. withdrew from the Treaty. So, for the export oriented part of Canadian agri-food, CPTPP is a substantial opportunity. Nevertheless, Canada faces tremendous competition from other exporters such as Brazil, Argentina, Russia and Ukraine, many of whose governments are making substantial investments in transportation and port infrastructure to assist their farmers' ability to move grain to market. Canada continues to operate with a rail transportation that was developed over 100 years ago.

It is a great first step to improve Canada's access to world markets, but it needs to be a fundamental component of a more general framework to improve the sector's overall competitiveness.

CTEAM Alumni *in the News*

Sharla George Photography

Brooks and Jen White

MB OYF Winners

AME would like to congratulate Brooks and Jen White of Borderland Agriculture for their success in winning the MB Outstanding Young Farmer for 2018. Brooks and Jen are 2015-17 CTEAM Alumni.

Farming in the very southwestern part of MB, with land bordering on both the U.S. and SK borders, they raise 600 bison and crop 5000 acres. Part of their vision statement is "Regenerate" with the main focus on the farm integrating bison production into a diverse cropping system, improving soil management by grazing the bison on the cropland.

AME wishes you all the best in November at the National OYF!

To learn more about Brooks, Jen and their farm business: ***www.borderlandagriculture.com/our-story***

Bob Ross Memorial Scholarship

"We are very honoured that Bob's dedication and commitment to farm management excellence are being recognized through this Scholarship. Bob was passionate about the value of the CTEAM program, and he would be very pleased that we are supporting the program and Canadian family farmers in his memory."

— Nancy Ross and Family

Applications for the Robert L. Ross Memorial Scholarship will be available in June. The scholarship gives a Canadian farmer the chance to attend the Canadian Total Excellence in Agricultural Management (CTEAM) program.

Robert (Bob) L. Ross was instrumental in inspiring and encouraging farm management excellence across Canada and the United States through his leadership and passion for the agricultural community. A dairy farmer and farm business consultant from St.Marys, Ontario, Bob fought a courageous battle with cancer, passing in March 2014.

In 2014, as a tribute to his passion, leadership and legacy, the Robert L. Ross Memorial Scholarship program was established by Agri-Food Management Excellence, Farm Management Canada and the Ross Family.

Eligible applicants must be more than 21 years of age and must demonstrate:

- A progressive operation and entrepreneurial spirit
- How the value gained from the program will be used
- To contribute to the farm business
- To contribute to the agricultural industry at large
- Why taking CTEAM interests you personally
- Passion for the industry

If you know someone who demonstrates the criteria above, please encourage them to apply. More information can be found at ***www.agrifoodtraining.com/bob-ross-memorial-scholarship1***

Is There A "Best" Machinery Strategy?

By Larry Martin

Country Guide's Editor asked whether we see a trend among people taking our management course, CTEAM, in machinery strategies. Behind the question is the idea that their experiences may be of value to others.

The reality is that many strategies exist, ranging from turning over the complement of equipment every year, to squeezing out every penny by holding it as long as possible and doing your own repairs and maintenance. In many cases, different strategies have been well researched and justified by analysis. In others, not so much: no question that there was a tendency for some people to be "metal petters", especially during and after 2008 – 2013 when grain prices peaked.

Interestingly, there can be justification for different strategies: a host of factors can affect strategy choice. Three examples are:

- Your access to people who can repair and maintain machinery: having the ability and availability substantially reduces the cost of maintaining older equipment, making it potentially more attractive than new for a longer period.
- The farther north you are, the more equipment you need: both planting and harvesting windows are limited the farther north is your farm. If you have substantial acreage, you need to have lots of equipment to plant as soon as you can get on the land in the spring so the crop is ready for harvest during the short harvest window. This argument is underscored by early snowfall the past two years.
- The relationship with your dealer may give you deals that are just too good to pass up, deals that are good for both of you. After one year of use during which the new technology doesn't break down, in part because you take great care of it, the trade-in value is tops and a flip doesn't cost much for that year of use. It's good for both because the dealer gets two sales margins in two years.

Appreciating the variety of these factors is, in fact, what led us to develop our machinery investment course. Listening to CTEAM participants discuss the range of factors, it became evident that there could be value in determining whether the factors are true or rationalizations for new pets or for keeping the old ones around.

The arguments spawned two aspects of the course that are fascinating. The first question that a number of alumni and others asked was, how do I decide how much equipment I should have, and whether I'm over capitalized?

Am I Overcapitalized?

This question is often addressed with the average value of equipment available on grain farms with different soil types. This may be a good indicator, but it has two limitations. First is the obvious: it may be useful for grain farms, but what about others? Second is that no study shows a relationship between machinery investment or operating cost per acre and profitability.

These issues led to an aspect of the work AME has been doing with BDO suggesting that the most profitable farms have machinery capital costs just under nine percent of revenue, while it's just over 15 percent of revenue for the least profitable. This is an annual difference of $60,000 per million dollars of revenue, a significant impact on the bottom line. It offers a good start toward a substantive answer to gauging over capitalization. The next phase of the BDO work to be completed later this year with a much larger number of farm records, will give a much better idea whether it is an appropriate measure and how it might vary by farm type.

Should I Buy, Lease, Rent or Keep What I Have?

This is the second major question, it's where individual circumstances come into play. These can include location (therefore, how much time is available for planting and harvest), availability and cost of labour, what products are produced, the specifics of the deal, whether new machinery improves productivity, how long may you keep it, what's its likely salvage value; your perception of risk, your financial position, interest rate… The list can be long.

These decisions include time and the time value of money because they deal with long lived assets. So, evaluation needs to be done in a capital budgeting framework. Using that framework with considerations of an individual's specific circumstances often leads to two conclusions about machinery strategy.

The first is that including individual circumstances means that there is no "best" machinery strategy: individual circumstances drive what's best.

The second and related outcome is that what often seems to be an obvious answer frequently isn't when the circumstances are included. For example, machinery leases may make sense when the surface suggests they don't. Or, a personal favorite from the course is the evaluation of building a shop. Many of us expected the proposal was a pet project that the farmer wanted to justify. A relatively thorough analysis of the project with the individual circumstances resulted in a 19% internal rate of return.

These considerations partially account for why there is no clear trend in the machinery strategies of farmers with whom we work. Some still need to do the analysis to make sure they haven't invested in pets that make them over capitalized. But there is never a guarantee that, without the analysis, the right strategy can be forecast.