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Producers' Decisions

Allen Prosch[1]

Summary and Implications

The business decisions pork producers make are extremely important. Decisions increase in importance at the same time they become harder to make. In business management studies, time has been devoted to learn how such decisions can be made. Less study has been expended on how producers currently make decisions. In the United States, family producers have traditionally made decisions with information they could gather independently. The ability to create decision making information is difficult. Producers need to remember the key success item — that of effective management led by sound decisions. The process of decision making involves skills and abilities that can be learned. Attitudes towards risk and perceptions of agriculture have influenced producers to make decisions that do not reflect just the economics of the production sector. Also, off-farm employment and federal program payments have an effect on farm exits and on those exiting the pork enterprise, but who remain in farming. Changing the perceptions and attitudes of these producers may enable good producers to become more positive about their future in the industry.

Introduction

The business decisions pork producers make are extremely important. Decisions increase in importance, at the same time, they become harder to make. Producers face a number of challenges in their operations that are not directly related to their ability to produce pork.

One important change occurring in agricultural production is the change in business strategies. In business management studies, time has been devoted to learn how such decisions can be made. Fewer studies have been made on how producers currently make decisions.

In the U.S., family producers have traditionally made decisions with information they could gather independently. Producers would have been able to try several approaches to production in the past, but now the capital required, both monetary and physical, the risk involved and the margin to be gained, do not allow for many errors. However, the decision

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framework is becoming more complex. Producers need to deal with more information than ever. The ability to convert an overload of data into decision making information is difficult. And, the business environment is less tolerant of errors. Also, there is additional uncertainty risk and competition associated with changes in the agriculture and food industries. These increase the need for farmers to make informed decisions and have a plan for their businesses.

Decisions Now Involve More Pprocesses

Traditionally, an operation's resources were primarily labor, buildings and equipment. Today, an operation's resources may include intangible assets such as marketing systems, decision-making processes, coordinating systems, and established patterns of production. These systems often have high volume sales and purchases, professional expertise, skilled and motivated managers, alternate access to equity and debt capital, and sophisticated risk management practices that add to their competitiveness. Therefore, producers of all sizes are asking if they are large enough. But, producers need to remember the key success item — that of effective management led by sound decisions.

Decisions Involve More Skills and Abilities

The process of decision making involves skills and abilities that can be learned. However, that management ability, especially on smaller operations, does not improve without outside support. When managerial ability is fixed, decisions are made that do not reflect the true economies of the operation. Thus the size of an operation appears to be a driving factor in success, but not for production reasons as much as for management reasons.

Producers' decisions can be influenced by factors that have little or no relationship to the outcome of the decision. Most notable is the dramatic reduction in the number of pork producers who have decided to exit the industry in the past 15 years. Producers leave the industry despite having operations that are cost effective. From 1989 to 2002, producers with a 125-sow farrow to finish operation, with average production, would have had four years out of 14 in which that enterprise would not have generated all of an average family living. While the amount of funds generated by the swine enterprise for other farm expense or reinvestment went down, those producers who quit did so despite having successful swine enterprises.

Producers exit the industry for a variety of reasons, including production, economic, educational, environmental, and social issues, many of which are intangible. Producers who quit production from 1992 to 1996 were surveyed in 1997. Those producers surveyed gave low prices as the number one reason for leaving the industry. However, 82% of the respondents said they did not know their cost of production. Of the 18% who did know, the average cost was $39.03. This value would have been below the average Iowa / Southern Minnesota market prices in all the years included in the survey. However, only 10% of these producers had operations that would have 125 sows. They reported only 40% of their livelihood was provided by the swine enterprise. One-third of the producers increased another enterprise to use their time, but 45% reported working fewer hours on the farm. Seventy-five percent of the swine facilities used by these producers were reported as of types that by 1992 were becoming obsolete. And 73% of the producers indicated they planned to destroy the facilities, rather than use them for any purpose. While low prices may have been the stated cause for the action in the producers mind, the economic outcomes, contributory income, use of assets, and use of time do seem to be highly important. Often economic decisions are thought to be driven by maximizing economic return. That does not appear to be the driver here.

In a survey of producer's decision making conducted in 1992, producers indicated that marketing was a weak point in their operations. They identified help with marketing as a critical need. However, among numerous financial resources they might use, they indicated strongly they would not hire marketing help. In other financial areas of equal importance and need, they indicated they would or do hire help. It appears that producers of all commodities are concerned with low prices, but activities to help improve those prices on the marketing side are not well accepted.

Decisions Are Influenced by Attitudes

In a 2002 report on producers' decisions involving off-farm work, it was found that attitudes about risk influence the decision. As a result of risk aversion, a producer was likely to diversify income through off-farm labor endeavors. While farmers engaged in livestock production were more likely not to seek off-farm work, largely due to the constant on-site labor demand, the 1997 survey showed that once having quit the livestock operation, one-third of the respondents increased their off-farm work. It was also found that the greater the scale of production, the less likely the farmer would work off farm. Smaller pork producers who felt prices for hogs were inadequate may have chosen to exit the industry and take the option of off farm employment because it was seen as less risky.

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In the mid-1990s, significant attention was given to forming networks of producers. It was thought that some of the value of larger systems could be captured by independent operations working together. In a 2002 report identifying independence as a decision influencing factor, it was found that even though the alternative may be profitable and less risky, not accounting for the value of independence would lead to underestimating the amount of profit necessary to attract farmers to such arrangements.

In a 2001 study of attitudes about profit and loss among another group of producers in an alternate farm enterprise, it was found that people tend to be about twice as upset about a loss as they would be happy about a gain of the same size. Looking back at low prices as the number one reason to exit the pork industry, this would support pork producers feeling much more discouraged by a few years of loss, despite numerous years of profit. Also contributing to this, in poor years the loss is often significantly larger than the yearly profit for better years. The dramatic difference has a greater impact on the attitude of producers than the actual economic reality. Producers also are affected by their attitude toward marketing tools used to improve prices. The combination of perceptions along with the attitude towards risk, affect the decision to participate in an enterprise.

A 2005 survey of producers involving the influence of weather and climate information showed the greatest improvement in use and influence of weather and climate forecasts will come from changing the individual's attitude. Again, an individual's perceptions of and attitudes about the information outweighed the application of useful information.

Final Thoughts

Producer decisions in the pork industry at the production level have been driven by factors other than economic return. As the industry has changed, diversified pork producers have responded to that change similar to other groups of farmer producers.

Attitudes towards risk and perceptions about the pork industry have influenced producers to make decisions that do not reflect just the economics of the production sector. Also, off-farm employment and federal program payments have an effect on farm exits and on those exiting the pork enterprise but remaining on the farm. These effects still exist. In a recent survey, 44% of producers still "feel" their future in the industry is severely threatened.

It is clear that many producers who are capable of competing in pork production feel threatened by change. Changing the perceptions and attitudes of these producers is a difficult task; however, doing so may enable good producers to become more positive about their future in the industry.

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