



# CHAPTER 6

## The Business of Cotton Farming



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# THE NATURE OF A COTTON FARM BUSINESS

ALL COTTON FARM BUSINESSES ARE DIFFERENT. THERE ARE LARGE CORPORATE FARMS, SMALL FAMILY FARMS, PUBLICLY LISTED COTTON AGRI-BUSINESSES AND A MIX OF EVERYTHING IN BETWEEN.

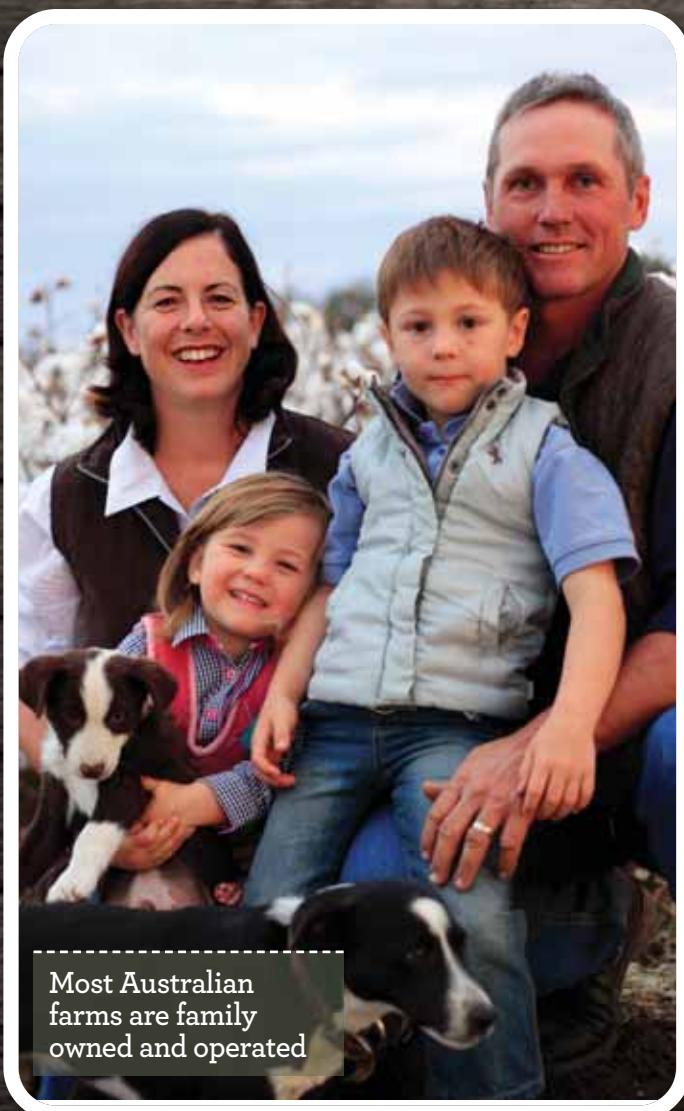
What we do know is that the average Australian cotton farm:

- Is family owned and operated
- Provides jobs for eight people
- Grows 467 hectares of cotton
- Is run by experienced farmers with an average age of 39
- Grows other crops and often grazes sheep and cattle

## GOALS OF A COTTON FARM BUSINESS

BECAUSE IN MOST CASES A COTTON FARM IS NOT JUST A COTTON FARM BUT GROWS OTHER CROPS AND OFTEN GRAZES SHEEP, BEEF OR OTHER LIVESTOCK, THE GOALS OF A COTTON ENTERPRISE VARY FROM FARM TO FARM.

- To grow high yielding cotton crops (so that there's more cotton to sell at the end of the season)
- To grow high quality cotton crops (to attract premium prices on the world market)
- To maximise profits across the farm operation
- To keep operating costs to a minimum
- To run an efficient operation
- To ensure a safe working environment for staff and contractors
- To minimise impacts on the natural environment



Most Australian farms are family owned and operated





# STAKEHOLDERS IN A COTTON FARM BUSINESS

- FAMILY
- WORKERS  
FULL-TIME AND PART-TIME
- CONTRACTORS  
(FOR EXAMPLE SUPPLY PICKING,  
AERIAL WORK, TRANSPORT  
COMPANIES AND AGRONOMY  
SERVICES)
- FINANCIAL INSTITUTIONS  
(BANKS, FINANCIERS)
- ACCOUNTANTS
- LAWYERS
- COTTON MARKETING  
ORGANISATIONS
- GINNING COMPANIES
- RURAL SUPPLY COMPANIES  
(EG SEED, FERTILISER,  
MACHINERY, FUEL)
- GOVERNMENTS THAT REGULATE  
THE BUSINESS OF FARMING
- INTERNATIONAL CUSTOMERS  
(EG SPINNING MILLS, CONSUMERS)

## COTTON GROWERS HAVE A LOT ON THEIR MIND!

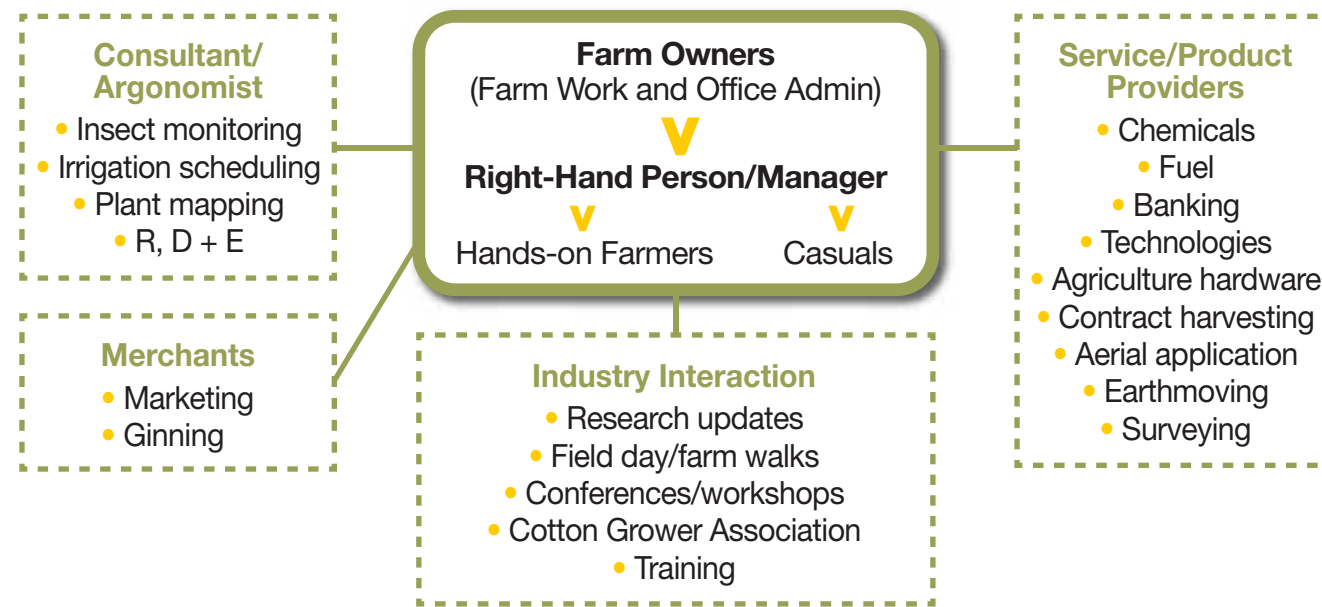




# ORGANISATIONAL STRUCTURE

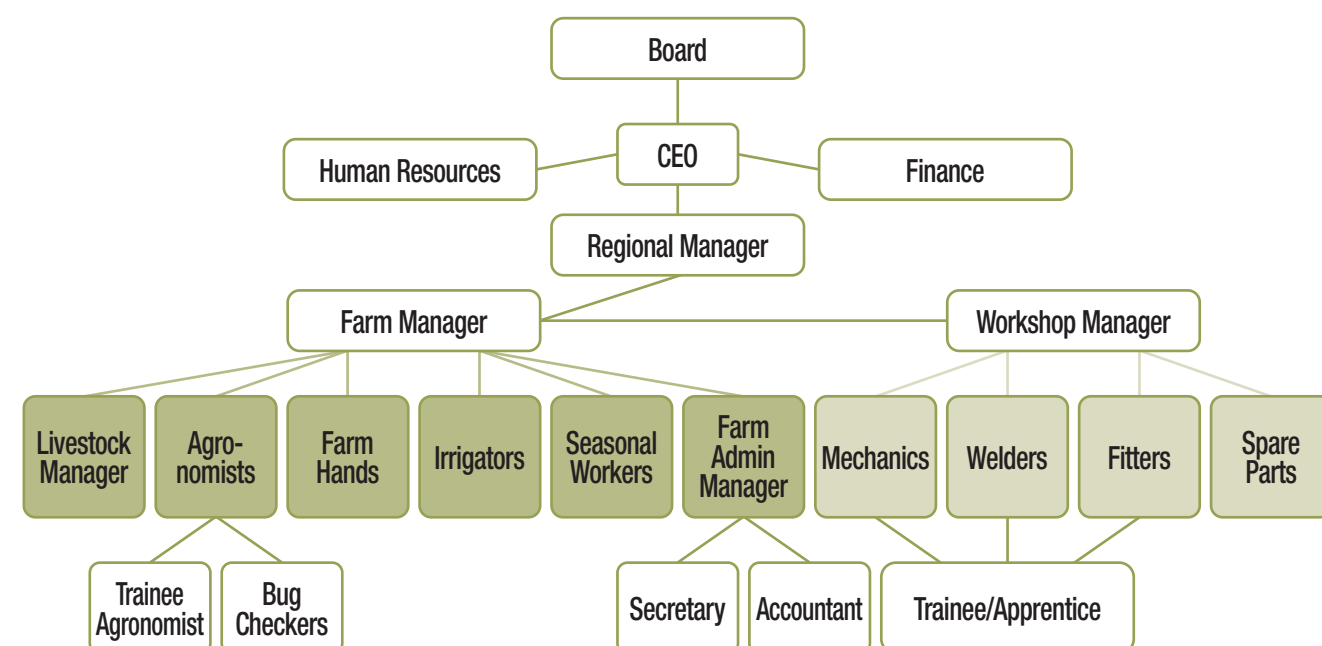
While every farm is different, the following charts gives an indication of the types of structures typical in a family owned and operated Australian cotton farm (this forms most of the industry) and also a corporate farm.

## FAMILY FARM STRUCTURE



**Farming duties:** GPS, irrigation, planting, cultivating, payroll, budgeting, plant operation, workshop, accounts, chemical application, OHS/WHS, human resource management, infrastructure repair and maintainance (channels, gates, roads, pumps etc.)

## EXAMPLE OF CORPORATE FARM STRUCTURE



## FACTORS TO CONSIDER WHEN GROWING A COTTON CROP

Cotton is a difficult crop to grow well and requires experienced farmers who pay lots of attention during the season. Cotton growers need to take into consideration a large range of factors to get high yielding, high quality cotton that is water efficient and can be sold for a top price. They must be great planners, innovators, managers and decision makers.

Considerations include:

- Government regulations
- Weather
- Sustainability
- Increased input costs
- High quality crops
- Occupational health and safety
- Business management
- Succession planning
- Technology upgrades
- Pest control
- Managing contractors
- Marketing
- Yields
- Consumer demand
- Disease control
- Farm labour
- Ginning contracts
- Training
- Equipment maintenance and upgrades
- Farm hygiene
- Time for family
- Community
- Transporting the crop
- Interest rates
- Crop selection and rotation
- Commodity markets
- New varieties
- Health and mental health
- Energy costs
- Climate change
- Finance
- Insurance
- Access to rural doctors
- Access to education
- Drought, floods



# THE MAIN BUSINESS FUNCTIONS OF A COTTON FARM

FUNCTION	FACTORS TO CONSIDER
SETTING UP THE FARM FOR COTTON PRODUCTION	<ul style="list-style-type: none"><li>• Costs associated with irrigation infrastructure, laser levelling of fields etc</li><li>• Commitment to cotton production – it’s a difficult crop to grow and the farmer must be equipped with knowledge and know-how in order to make it work from a business perspective</li></ul>
FINANCING YOUR CROP	<ul style="list-style-type: none"><li>• Relative to other summer crops, the costs of growing cotton is higher</li><li>• Farm budgeting is essential</li><li>• Finance must be arranged with banks/lending organisations or arrange for crop credit well prior to planting (before ordering seed)</li><li>• Hail presents a significant risk to summer crop production including cotton. This may affect the financial position in relation to growing costs and marketing positions. It is important that hail insurance coverage is discussed with an experience broker in cotton insurance</li></ul>
OPERATIONS	<ul style="list-style-type: none"><li>• The cost of production</li><li>• Inputs and outputs</li><li>• All of these must be carefully budgeted and planned for</li></ul>
HUMAN RESOURCES	<ul style="list-style-type: none"><li>• Attracting and retaining staff</li><li>• Engagement and conditions of employment and management</li><li>• Training</li><li>• Safety</li><li>• Working with contractors</li><li>• Relationships with neighbours</li></ul>
SELLING THE CROP/MARKETING	<ul style="list-style-type: none"><li>• Cotton has unique marketing parameters based around fibre quality</li><li>• Premium and discount sheets should be discussed with an experienced cotton merchant/marketer</li><li>• Current state of the world market for cotton (supply and demand)</li><li>• Current world prices</li><li>• Forward-selling of cotton crops can occur before crops are sown, up to three years in advance – this needs to be planned for</li></ul>

## HUMAN RESOURCE MANAGEMENT



Attracting and retaining an on-farm workforce is a critical part of the farm business

The Australian agriculture sector is currently experiencing a labour and skills shortage, driven by an aging workforce, low attraction rates and strong competition from the resource sector. This is being felt in the cotton industry, which is facing the challenge of attracting and retaining core staff, on- farm labour (unskilled and skilled), and access to professional advisers and service providers.

The problem has recently been driven by rapid expansion of the industry following years of drought, and the resources boom in some regions. Other factors such as poor public perception/image of rural towns, lifestyle and work are also thought to contribute to the problem.

Given the current skills and labour shortages, many growers are relying on overseas workers to fill gaps. Overseas workers have played a small but important part in the Australian agricultural industry for quite some time, helping farmers at peak times when local labour is difficult to access.

Whilst skilled migration can deliver labour for emerging shortages in short time frames, it can only complement Australia’s domestic training arrangements which must deliver the backbone of Australia’s skilled labour needs. For the cotton industry, a commitment to our local workforce and communities remains a priority.

Cotton growers attract employees using a range of tools including word-of-mouth, employing school students as schools based trainees, using recruitment specialised labour hire companies and internet sites such as gumtree.com.au or head-hunting promising employees. They use a range of strategies to retain staff which may include attractive salary packages, training, flexible working arrangements, mentoring, opportunities to have a stake in the business and/or promotion.

The cotton industry’s labour force is critical to sustaining the industry’s competitive advantage. Innovative, resilient and adaptive people, businesses and communities are crucial to the future success of the industry and needs to be supported by processes for attracting, retaining and developing people.

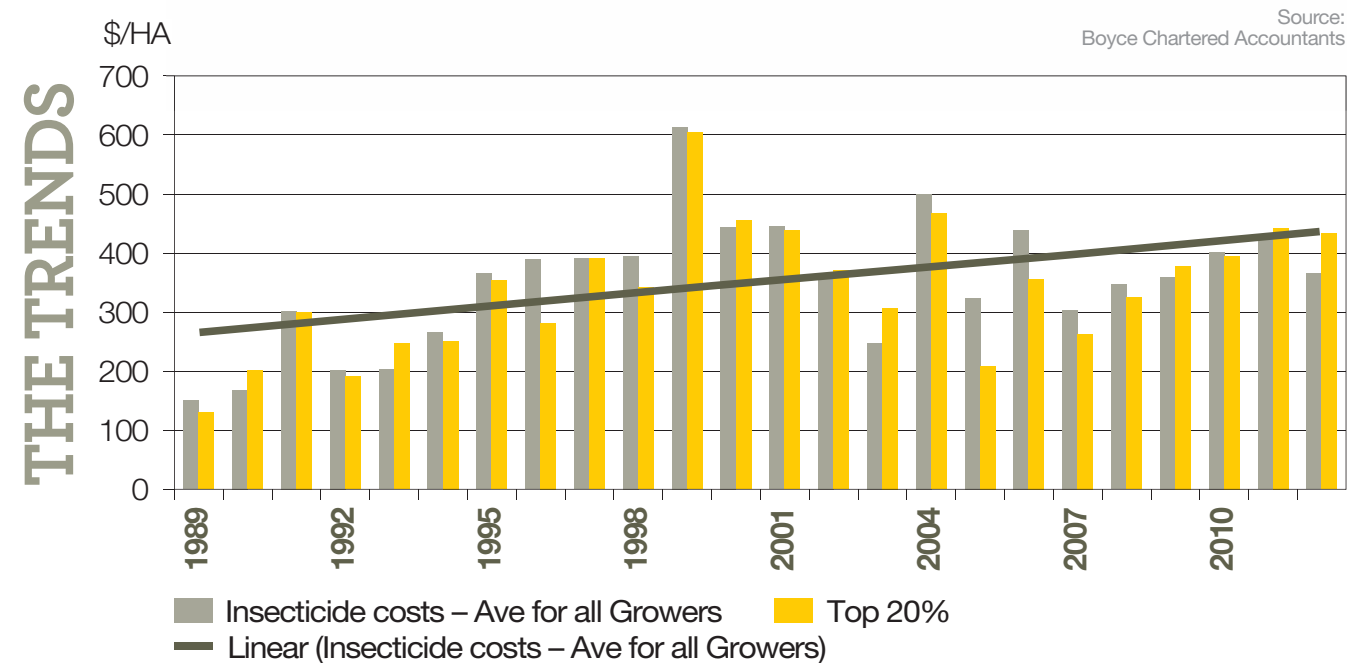
The cotton industry’s labour force takes into account on-farm labour, as well as the service industry and supply chain, which represent an extensive network of input and advisory providers that support cotton farmers such as agronomists, researchers, consultants, agribusiness, State government agencies, Cotton Australia, CSIRO, and universities. The dynamics of the industry’s labour varies depending on factors such as season, location and business size.

# THE COST OF PRODUCTION

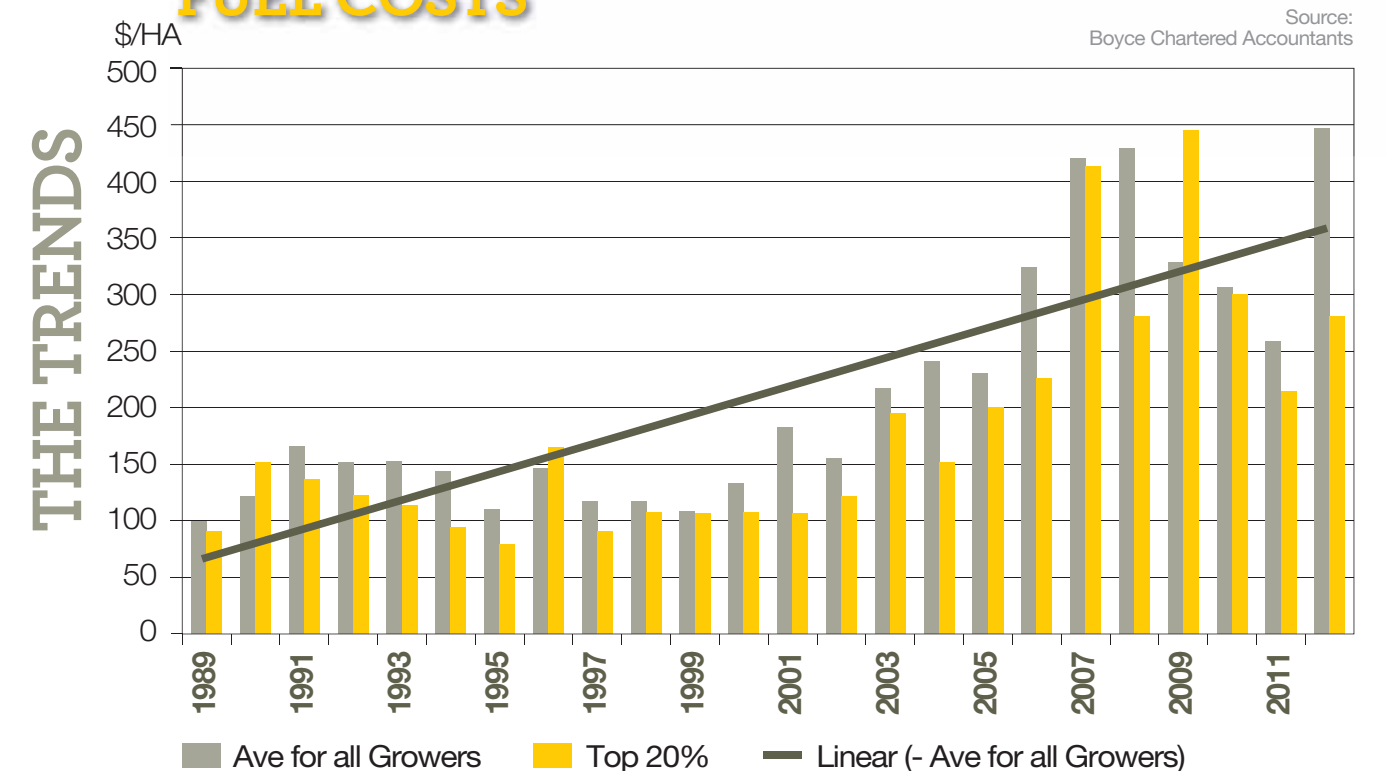
Cost of production is a very important factor in making a cotton farm business profitable. Cotton growers work hard to minimise their costs of production in order to maximise profits. Unfortunately, the cost of production is continually on the rise and this, coupled with the fact that Australian cotton growers pay premium prices for inputs (due to geographic isolation) means that growers need to always be looking for ways of becoming more efficient. Rising costs of production is a major issue facing Australia's cotton growers.

Below are a series of graphs illustrating the rising costs of production for Australia's cotton growers.

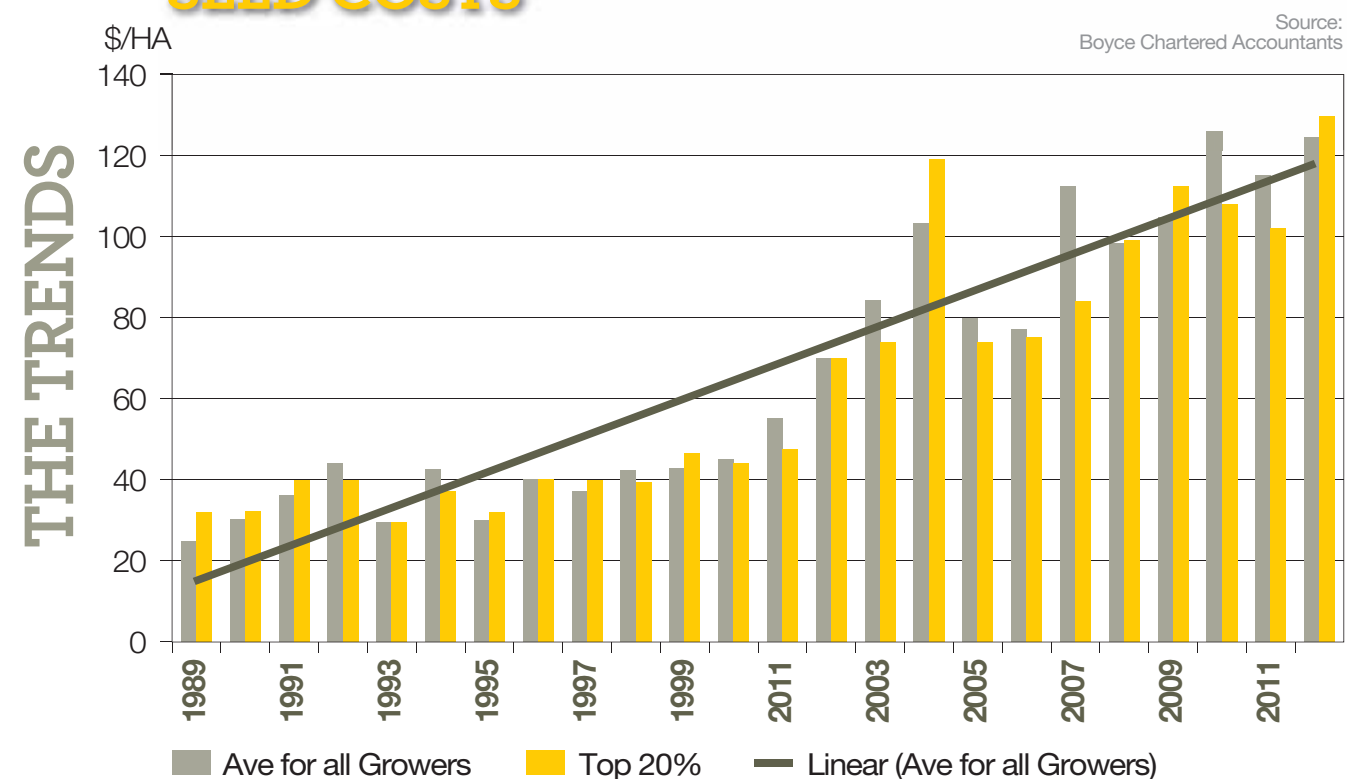
## INSECTICIDE AND BOLLGARD COSTS



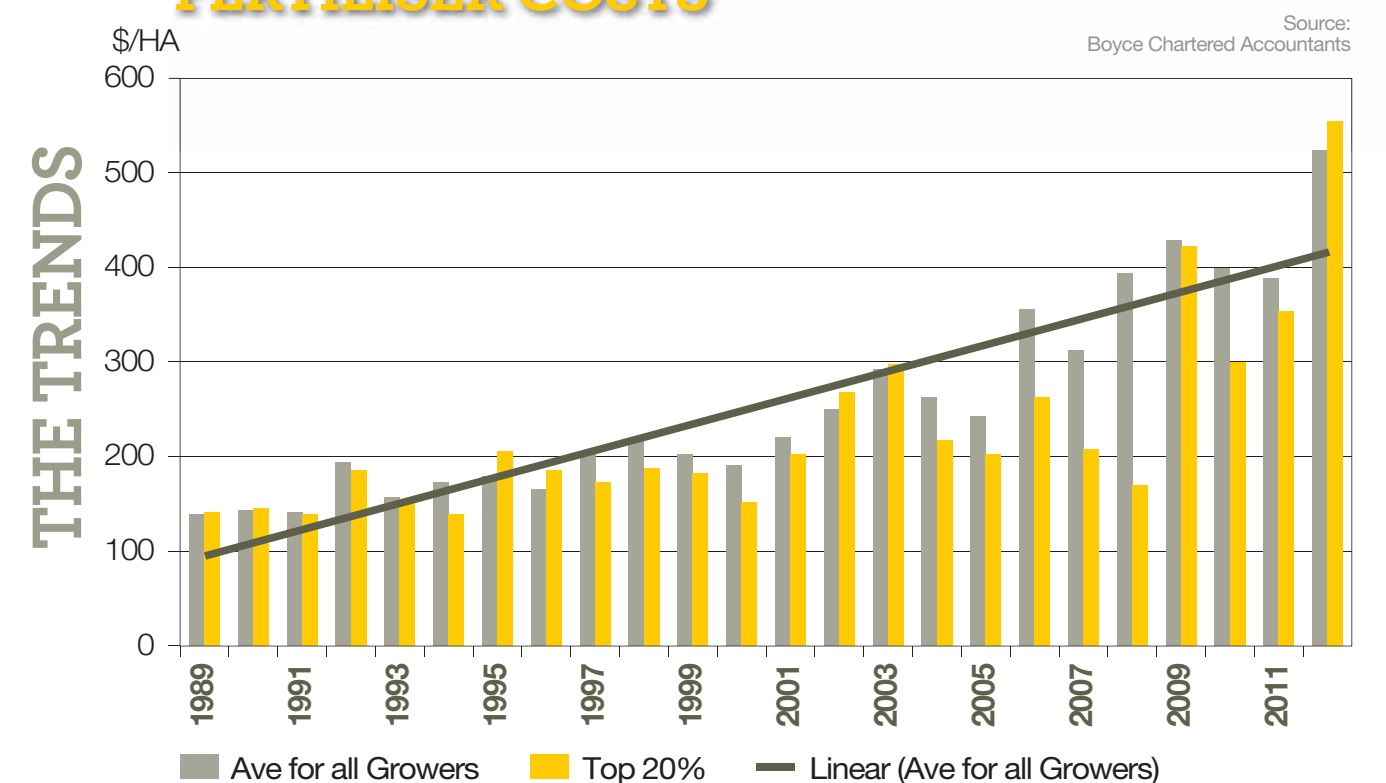
## FUEL COSTS



## SEED COSTS



## FERTILISER COSTS





# OPERATING COSTS & PROFITS \$

To manage costs of production, cotton growers develop detailed farm budgets that detail operating costs and expected profits. These are based on experience and historical data, local information as well as information provided by the cotton industry and government departments. Costs vary year to year and even season to season, so these budgets need to be updated regularly to make sure everything is on track for a profitable season.

The graphs on this page show some data relating to operating costs and profits for an average Australian cotton farm. Please note however that numbers vary widely from farm to farm.

## THE AVERAGE FARM

### CASHFLOW PERFORMANCE:

Gross Income	4,800,000
Operating expenses	<u>3,500,000</u>
Operating surplus	1,300,000
Interest	<u>600,00</u>
Net profit	700,00
Drawings – personal, school fees etc	<u>150,00</u>
Balance available for income tax, plant purchases, debt reduction or investment (Seed capital)	<u>\$550,000</u>

(Source: Boyce Chartered Accounts)



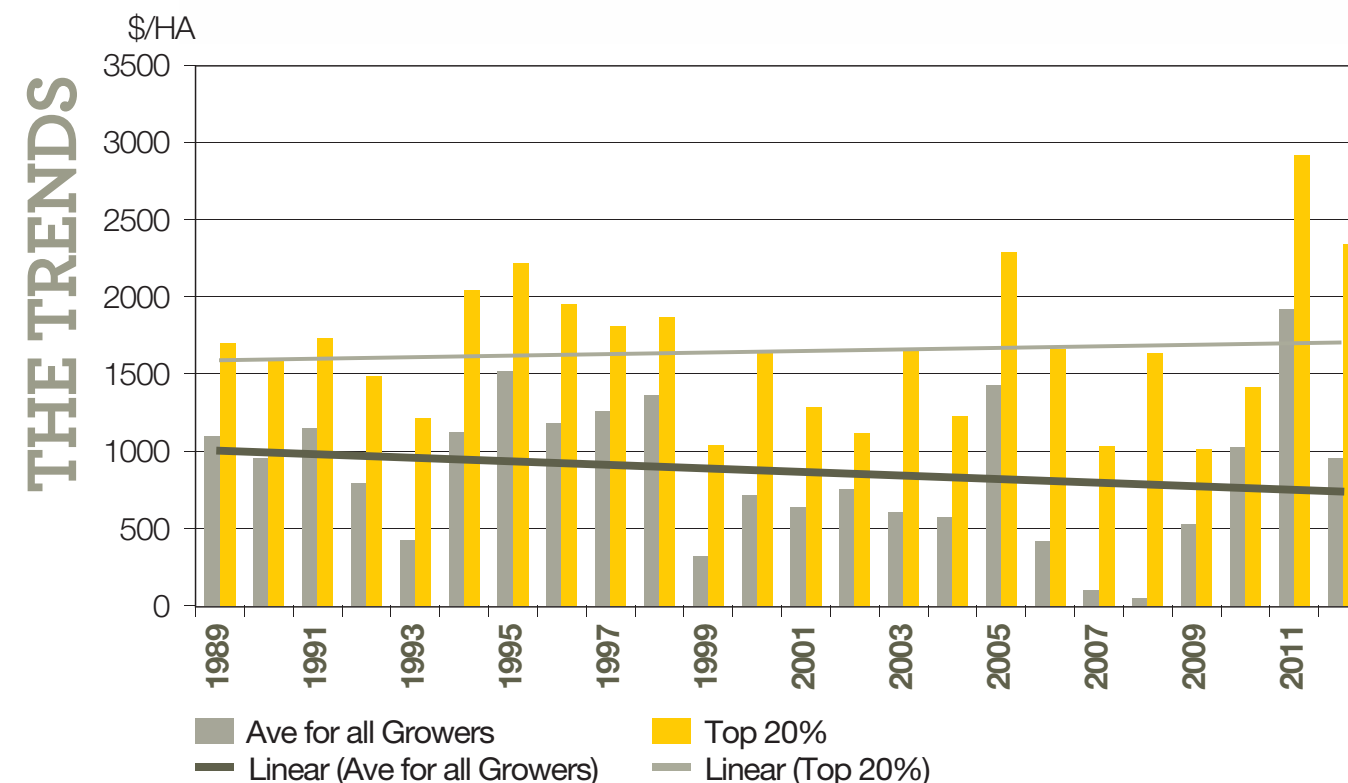
A typical irrigated cotton Farm Budget for Northern NSW



A typical dryland (rain grown) cotton Farm Budget for Northern NSW

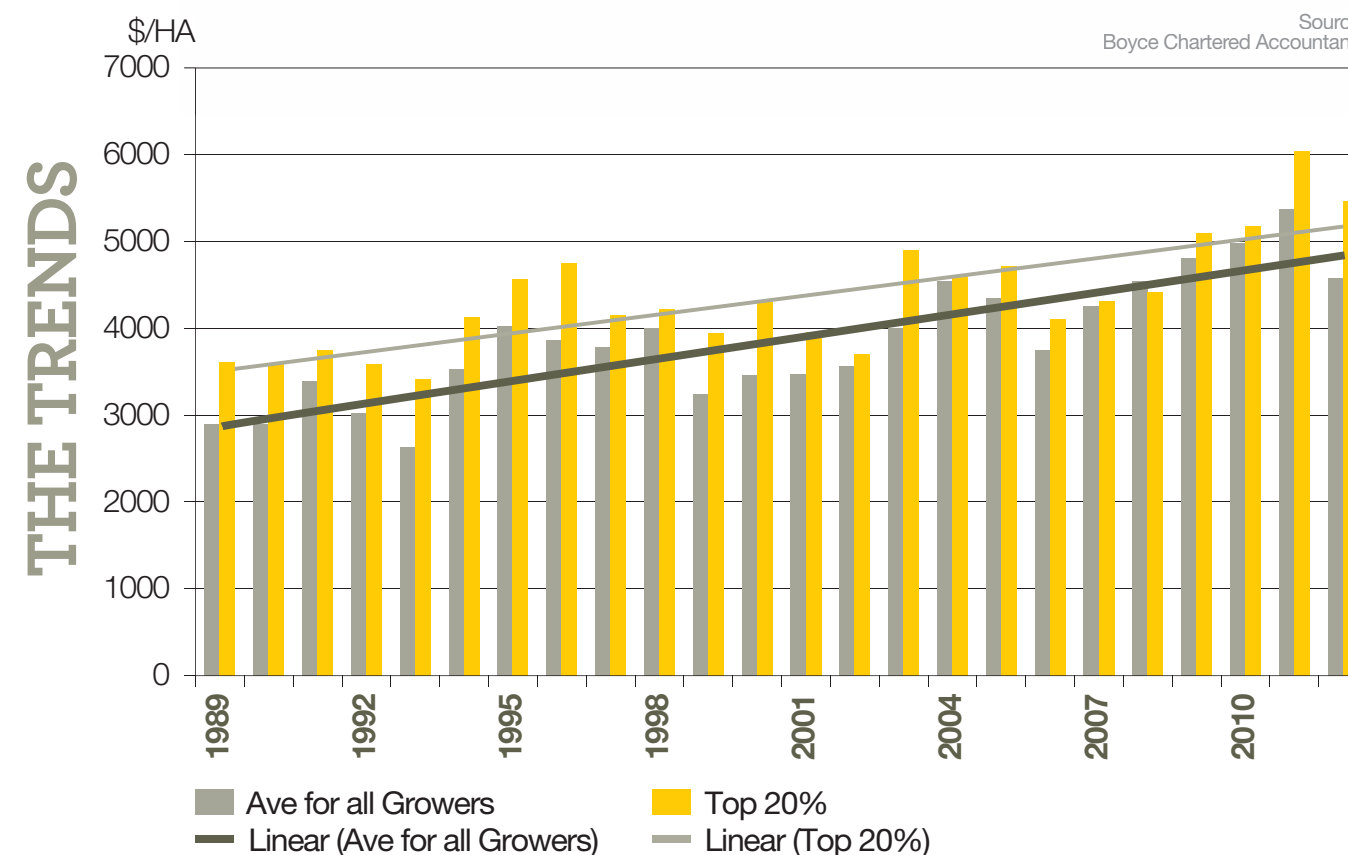
## OPERATING PROFIT BEFORE INTEREST

Source:  
Boyce Chartered Accountants



## TOTAL INCOME

Source:  
Boyce Chartered Accountants





# PROFITABILITY

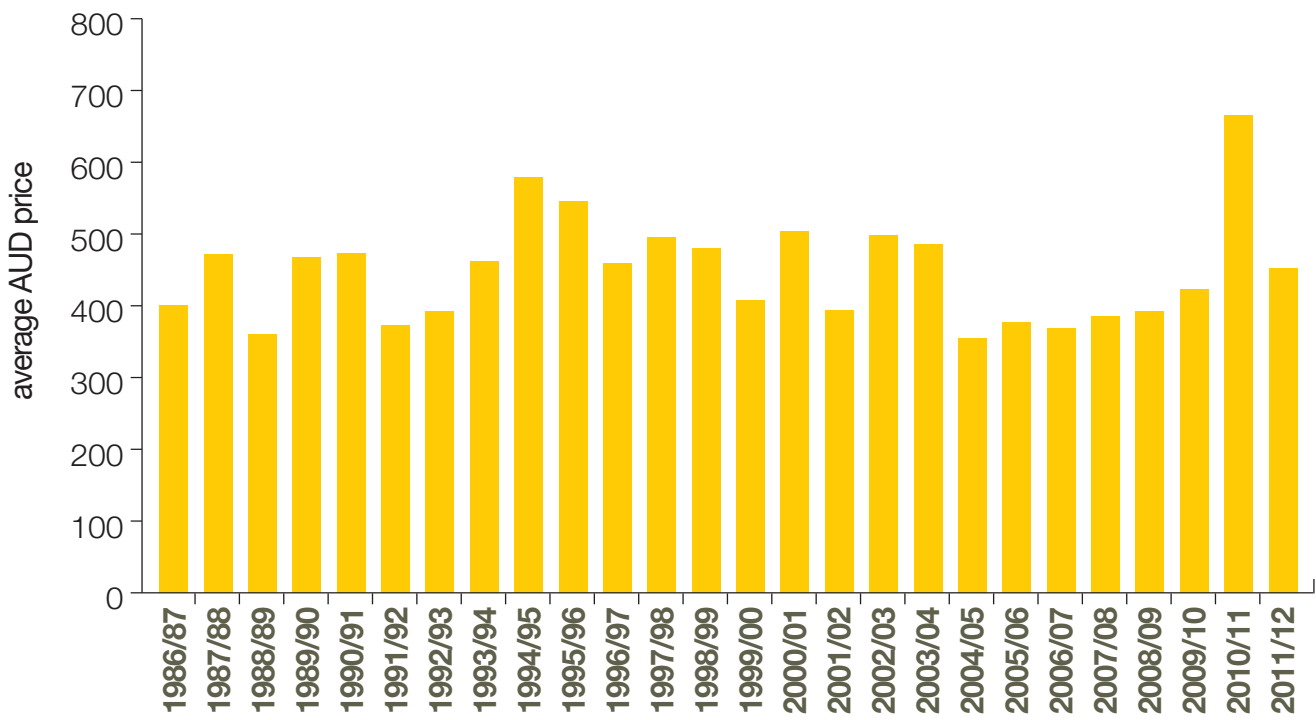
For the cotton farm to be profitable the grower needs to maintain high yields and minimise costs. That means farming carefully by constantly monitoring water needs and use, pest numbers and such things as soil quality. It also means developing and implementing good marketing strategies for selling cotton into the world market. For irrigated

cotton the availability and cost of water is one of the key factors influencing profitability.

# WORLD PRICES

World prices for cotton fluctuate daily according to world demand and supply and can vary from season to season between approximately \$350 and \$600 per bale for Australian cotton.

# AUD BALE PRICE – AVERAGE ANNUAL



# MARKETING

Australian raw cotton is marketed under a competitive market system with several major international and local cotton merchants operating in the Australian market. Cotton growers have a range of options for the delivery, processing and sale of their cotton, including:

- Sell directly to a merchant or ginner (also known as a processor). The grower sells the cotton before it has been processed. The merchant or ginner then sells and ships the seed and lint separately
- Deliver to a ginner who retains the cottonseed, with the grower receiving the lint to be sold separately via international markets
- Grower retains ownership of both cottonseed and lint and, after paying a processing fee, sells both cottonseed and lint independently

# PRICE OPTIONS

A number of factors can influence the price of cotton. These include the amount of cotton available for purchase (i.e. how much cotton growers supply to the market) and the quantity of cotton that processors need or wish to purchase (i.e. the amount they demand). The price is also dependant on the futures price on the New York Stock Exchange and the exchange rate of the US dollar.

Farmers can choose to sell their cotton lint in a number of ways:

- Cash market** — The price of cotton on world markets fluctuates daily. When growers have cotton ready for sale, they can sell it at the daily or 'spot' price.
- Forward contract** — Using the cash market involves a certain amount of price risk, i.e. that the spot price will fall when the grower is ready to sell. To help insure against this risk, the grower can negotiate a forward contract with a buyer. This agreement sets out the price, quantity and quality of cotton the grower has to deliver on a specified future date. Therefore, the grower can know how much the crop can be sold for even before it has been planted.
- Seasonal pool** — Growers commit a certain proportion of their cotton production to a pool of cotton. An agent is responsible for selling the cotton in the pool on behalf of all the growers. The price received by the growers for their cotton is the average of all sales made from that pool in that season.
- Minimum price pool** — ensures that the farmer gets at least the seasonal pool price. If the prices go higher growers receive higher fees.

- Call pool** — farmers must promise an amount of cotton for the pool but this cotton can be traded using 'futures' and 'options' methods of sale, where amounts traded are simply written down as potential sale orders on paper.
- Balance of crop** – bales not sold using any of the above methods are sold at an agreed price.

# COTTONSEED MARKETING

Cottonseed is marketed differently to the fibre. Growers have two options when selling their seed:

- They may sell it to a company that has a 'seed pool' (a stockpile of seed purchased from a number of different growers). This type of company either sells the seed as stock feed, or crushes it to make oil.
- Growers can sell their seed to small private traders who on-sell the seed here in Australia or overseas.

Some growers grow a portion of their crop purely for planting seed — the seed used to plant future crops. Planting seed is specially grown under contract to seed companies. The emphasis is on producing healthy, high quality seed rather than lint. Growers must ensure that there is no contamination by weeds or cross breeding with other varieties of cotton. These crops are picked and ginned separately to maintain purity in the different varieties.