financial performance of farms in Southern Central Western Australia

Thuy Van Mellor, Peter Martin, Phantipa Puangsumalee, Vernon Topp and commodity analysts

In this paper, Southern Central Western Australia has been defined to include 29 Western Australian shires extending from Denmark to Esperance in the south to Pingelly and Kulin in the north (map 1).

regional profile

Southern Central Western Australia is heavily reliant on wheat production. Wool production, sheep, lambs, barley and canola also make a substantial contribution to the total value of agricultural production. In addition, a large variety of other agricultural products, including wine grapes, strawberries, milk, fruit and cut flowers are produced in the higher rainfall southern coastal areas.

The region typically produces between a quarter and a third of Western Australia’s total value of agricultural production, depending on the size of the region’s grain crop. The gross value of production from the region was estimated at around $1.8 billion in 2003-04. Wheat generally accounts for around one third of the gross value of agricultural production and wool has historically been the next most important commodity. In 2000-01, wool contributed 20 per cent of the gross value of agricultural production, but by 2003-04 this contribution had declined to 15 per cent, a similar percentage to that contributed by barley. Over the same period, sheep and lamb sales have increased their contribution from around 9 per cent in 2000-01 to around 11 per cent in 2003-04.

The agricultural sector is the second most important provider of employment in Southern Central Western Australia. According to 2000-01 employment statistics from the Australian Bureau of Statistics, the agriculture sector employed 19 per cent of the workforce, or 14,900 people, in 2001, around 1000 less than the number employed in the retailing sector (figure B).
broadacre farm performance

In this section the financial performance of broadacre farms in Southern Central Western Australia is considered, along with the performance of broadacre farms in Western Australia as a whole and nationally.

Broadacre farms account for 93 per cent of farms in Southern Central Western Australia (table 1). The broadacre sector of agriculture is defined to include five industry types: wheat and other crops, mixed livestock–crops, sheep, beef and sheep–beef. In simple terms, broadacre farms are those that run beef cattle or sheep or grow grains, pulses or oilseeds or some combination of these activities. According to the Agricultural Census conducted by the Australian Bureau of Statistics in 2001 there were 4940 farms in this region, of which more than 63 per cent were either mainly dependent on grain growing or combined grain growing with production of livestock, usually sheep. This share was significantly higher than the national average of 23 per cent (table 1). Only 10 per cent of farms in the region are mainly dependent on beef cattle, significantly lower than the national average of 24 per cent. Almost all beef farms in the region are relatively small in terms of their agricultural output.

While the region has a substantial number of relatively small farms (around 40 per cent of the region’s farms have a value of agricultural output of less than $150 000), the majority of the region’s agricultural production occurs on medium and large sized farms (figure C). More than 70 per cent of the total value of agricultural production occurs on farms that have a value of agricultural production exceeding $300 000, and just under 50 per cent of the value of agricultural production is from farms with a value of agricultural production of more than $600 000.
Nationally, the financial performance of Australian farms was better in the three years to 2005-06 than during the drought of 2002-03. From 2003-04 to 2005-06, prices for livestock remained high in historical terms, assisting farms to manage cash flow during a time of reduced production. High beef cattle prices in recent years, in large part a consequence of increased sales to the Japanese market, have been particularly important in maintaining farm incomes as more Australian farms engage in beef cattle production than in any other enterprise.

On the back of record winter crop receipts in both Western Australia and South Australia and high livestock receipts, farm cash income for the broadacre industries as a group increased in 2003-04 from the drought reduced income in 2002-03 to be slightly above the long term average in real terms. However, in 2004-05, grain production was again reduced by drought and in combination with lower grain and wool prices led to a fall in average farm cash income for broadacre farms. Increased winter rainfall across most of Australia’s grain producing regions in 2005 led to a recovery in winter grain production and an increase in farm cash income in 2005-06 in southern mainland states. Cash receipts are expected to rise nationally in 2005-06 although this is forecast to be offset by an increase in farm costs resulting mainly from higher oil prices, together with lower wool prices and, in some states, reduced beef cattle turnoff, so that average farm cash income is expected to decrease slightly (figure D).

**Return to capital**

Strong demand for rural land over the past four years has increased the value of farms’ capital base and this has underpinned strong farm equity positions. Rising land values have, so far, largely offset the impact of higher farm debt on farm equity, as some producers borrow for working capital to meet reduced cash flow during the drought and as others borrow for farm expansion and investment. Higher farm capital values have resulted in reduced rates of return excluding capital appreciation, but have led to historically high rates of return including capital appreciation.
broadacre farm performance – Western Australia

Historically, farm cash incomes for Western Australian broadacre farms have exceeded the national average. In part, this is a consequence of the larger average enterprise size of Western Australian farms, compared with broadacre farms nationally.

Over the past decade, the pattern of change in farm cash income for Western Australian broadacre farms has been similar to that occurring at the national level. The exception was in 2000-01 when a poorer cropping season in Western Australia led to a sharp drop in the average level of farm cash income in the state. Recent changes to average farm cash incomes on broadacre farms in Western Australia have also been influenced by changes in pool payments for grain crops, particularly since 1999-2000 when harvest loans were introduced. For example, record winter crop production in Western Australia led to very high farm cash incomes in 2003-04. Many grain producers in Western Australia opted to receive a substantial proportion of the receipts from the 2003-04 crop in 2004-05. As a consequence, the average farm cash income for broadacre farms in Western Australia in 2004-05 was higher than would be expected based on the reductions in crop production and prices.

In 2005-06, farm cash incomes for Western Australian broadacre farms are estimated to have fallen slightly to average $97 000 a farm, still well above the national average of $62 000. Increases in crop receipts resulting from a larger winter grain crop in 2005-06 in Western Australia relative to 2004-05, were moderated by lower wheat prices and reduced pool payments from the smaller 2004-05 wheat crop. In addition, reduced beef cattle turnoff and lower wool prices reduced receipts on many livestock farms, despite higher sheep and lamb turnoff. Increases in farm costs exceeded the increase in farm cash receipts resulting in farm cash income falling slightly.

grains industry farms

Following the drought affected crop in 2002-03, farm incomes rebounded strongly in Western Australia, as in Victoria and South Australia in 2003-04, while crop production remained below average in southern New South Wales and Queensland. Record winter crop production in 2003-04 in Western Australia combined with relatively strong grain prices to result in very high farm cash incomes. In 2004-05, crop production in Western Australia was reduced by variable seasonal conditions, with frost and dry conditions occurring in many parts of the state.

In 2005-06 increases in crop receipts in Western Australia resulted from increased production of wheat, barley, canola and lupins relative to 2004-05, although the increases were tempered by lower wheat prices, and lower pool payments.

box 1: farm performance measures

Farm cash income is a measure of the cash funds available for farm investment and consumption after paying all costs incurred in production, including interest payments but excluding capital payments and payments to family workers.

A longer term measure of profitability that takes account of capital depreciation and changes to inventories of livestock, fodder, grain, wool etc is farm business profit. Farm business profit for broadacre industries is also estimated to have improved in 2005-06 and by a slightly larger amount than the increase in farm cash income due to an increase in inventories of livestock and grain on farms.
from the smaller 2004-05 average wheat crop. Increases in farm costs exceeded the increase in farm cash receipts resulting in farm cash income falling slightly. Despite the reduction, incomes remain relatively high in historical terms (figure E).

**sheep industry farms**

Overall, the financial performance of Australian sheep industry farms is estimated to have improved slightly in 2004-05, despite a fall in receipts from wool. Receipts from the sale of sheep and lambs and a reduction in expenditure on sheep purchases are estimated to have more than offset lower wool receipts, resulting in average farm cash income rising, but remaining below the longer term average.

Farm cash incomes for sheep farms in Western Australia mostly follow a similar trend to that observed nationally (figure F), despite there being some distinct influences on the Western Australian sheep industry. In particular, Western Australian sheep farms typically sell a higher proportion of their sheep for live export. More than 80 per cent of the sheep sent for live export from Australia in 2005 were sourced from Western Australian farms. In 2005-06, farm cash income for Western Australian sheep industry farms exceeded that recorded nationally, partly because of the larger scale of sheep industry farms in Western Australia, better seasonal conditions in southern Western Australia and relatively high sheep and lamb turnover. However, farm cash incomes in pastoral areas have generally remained low following substantial destocking during 2002 and 2003.

**regional farm performance**

Over the past two decades, average farm cash incomes for broadacre farms in the Southern Central Western Australia have generally been above the national average, but more variable from year to year. As noted earlier, the exception was in 2000-01, when seasonal conditions in Western Australia were poor, and average farm cash income in the region fell substantially.

However, the financial performance of broadacre farms in the region has not been as good as other Western Australian regions during the past 2 years, with a greater reduction in average farm incomes and lower rates of return to capital (excluding capital appreciation). Nevertheless, growth in land values in the region has remained strong, leading to historically high rates of return including capital appreciation (table 2).

**investment and land values**

Improvements in farm financial performance during the 1990s resulted in a steady increase in the real value of broadacre farm land in Western Australia (figure H). However, following a series of lower income years in the
late 1990s, the growth in land values eased. With the recovery in farm incomes in 2001-02 at the same time as the boom in urban property values, agricultural land values in Western Australia rose strongly, peaking at around $280 a hectare across the state.

While land values have historically fallen during prolonged periods of low farm cash incomes, land values have rarely fallen because of shorter term adverse seasonal conditions, such as short term drought or frost (as in 2000-01). However in recent years land values in Western Australia have continued to rise, despite a decline in farm incomes. A divergence between land values and farm incomes is unlikely to be sustained over the longer term.

### Commodity Forecasts

ABARE’s assessment of the outlook for world economic growth is provided in Australian Commodities, ABARE’s quarterly commodity forecasts and issues journal. Also included in Australian Commodities are market forecasts and detailed discussions of major Australian agricultural, minerals and energy commodities. A copy of the June quarter issue of Australian Commodities is included in delegate satchels. Below are commodity forecast summaries for a number of the commodities important to this region.

### Seasonal Update

The Australian Bureau of Meteorology in its latest seasonal rainfall outlook (25 July 2006) for the August–October period indicates there is a strong shift in the odds towards below average rainfall across north eastern Australia. Across the rest of the country the chance of accumulating at least average rainfall is close to 50 per cent.
The latest temperature outlook (25 July 2006) indicates that there is a shift in the odds towards above average day and night time temperatures for the August–October period. Across most of Western Australia there is a 60–70 per cent chance of exceeding both the maximum and minimum average temperatures.

grains

A forecast reduction in world wheat supplies, particularly in the United States as a result of poor seasonal conditions, is forecast to result in increased wheat prices in 2006-07. In July 2006, the world wheat price averaged US$211 a tonne, US$62 a tonne higher than in July 2005. Reflecting movements in world wheat prices, the APW 10 pool return for Australian growers is forecast to rise by 19 per cent to $223 a tonne in 2006-07.

World corn and soybean prices are forecast to be higher in 2006-07, reflecting strong global demand for these products, reduced global corn production and largely unchanged oilseed supplies. As a result, barley and canola prices in Australia are forecast to average around 8 per cent and 4 per cent higher respectively.

Persistent dry conditions across most of the Australian grains belt at the time of sowing are estimated to have resulted in the area sown to winter grains and oilseeds decreasing to around 20 million hectares in 2006-07, compared with 21 million hectares in 2005-06. The areas sown to wheat and barley are estimated to have been 5 per cent and 8 per cent lower respectively. In June ABARE forecast that Australia’s winter crop production would decline by 11 per cent in 2006-07. With most of the grains belt in need of rainfall in early August it is likely that winter crop production forecasts will be reduced.

In Western Australia, dry conditions during April–June have resulted in a reduced area sown to winter crops. With below average rainfall across most of the Western Australian grains belt in July and no significant falls in early August, winter crop production is forecast to be lower than in 2005-06.

beef

With Australian exports to Japan, the Republic of Korea and the United States likely to come under increasing pressure because of the return of the United States to export markets, Australian beef exports to other markets, such as Canada and south east Asia are likely to become more important. However, as this switch in export demand away from the high valued Japanese and Korean markets occurs Australian saleyard prices are forecast to weaken. Saleyard beef prices are forecast to fall 10 per cent to average 290 cents a kilogram in 2006-07.

The partial resumption of beef trade between the United States and Japan commenced in August 2006. US beef sourced from cattle 20 months and younger can now be imported into Japan. In the short term, the growth in Japanese imports from the United States will be influenced by the US industry’s ability to supply to specification and Japanese consumers’ perceptions of the safety of US beef products. Australia’s total beef exports are forecast to increase by 3 per cent to 915 000 tonnes in 2006-07.

With the continued retention of cows and heifers from slaughter over the past year, the Australian cattle herd is estimated to have increased to 28.5 million by June 2006. However, with prices forecast to ease in late 2006 and into 2007, the impetus for continued herd rebuilding is expected to ease and slaughter rates to increase. Cattle numbers are forecast to be 29.2 million by next June.
sheep meat and wool

Reflecting strong competition from alternative fibres and little growth in wool demand, the eastern market indicator price is forecast to fall 3 per cent in 2006-07, to average around 680 cents a kilogram.

The Australian sheep flock is forecast to grow slightly in 2006-07 to 104 million by June 2007. This is because relatively high prices for both lamb and mutton in 2005-06 have provided an incentive for producers to increase supply of sheep meat in 2006-07.

In 2006-07, the Australian saleyard price for lambs is forecast to average 8 per cent lower at around 320 cents a kilogram dressed weight, reflecting lower domestic demand for lamb as a result of strong price competition from other meats, especially beef, and increased lamb production.

Assisted by lower prices, exports of Australian lamb are expected to rise by about 14 per cent to 165 000 tonnes shipped weight in 2006-07. Live sheep exports are also expected to rise — by about 13 per cent to 4.5 million in 2006-07 as shipments to Saudi Arabia and the Middle East continue to return to the high levels experienced in 2002-03.