Variable order sharemilker

Description

A contractual arrangement where the farmer managing the property is paid on a percentage of milk income e.g. 23%.

How it works

These agreements are similar to contract milking agreements where the milker provides the labour, shed costs, electricity transport and sometimes a share of feed and nitrogen costs. The key difference is the milker is paid an agreed percentage of the milk income as opposed to a set rate per kgMS produced. These VOSM agreements are governed by the Variable Order Sharemilking Agreements Order 2011, and as such have less flexibility than a CM. No alteration to the agreement can be made if it is seen to be detrimental to the sharemilker under this order.

The VOSM payment method can be very profitable for the milker at high milk payouts but is vulnerable to a low payout. Recent milk price low levels resulted in many VOSM businesses becoming unviable and moving to other payment structures.

Advantages and considerations

Advantages

Variable Order Sharemilker

- Sharing profit and production can provide a significant equity boost in high payout years.
- Low equity required to get into business

Farm owner

- A VOSM shares production and payout risk and has a vested interest in the profitability and sustainability of the farm
- Reduces the level of day-to-day input into the farm

Considerations

- Will the VOSM business survive a low milk price? Protection mechanisms can be built into agreements.
- A minimum percentage share is set for herds under 300 cows. The terms of the agreement can be difficult to change.

Keys to success

- The farm owners and the VOSM should agree in principle a basic annual farm plan including expected fertiliser, nitrogen and supplement feeding inputs. This will ensure both parties understand what inputs can be expected throughout the season and have confidence in the milk production target.
- Good budgeting is essential to understand the costs and profitability of the VOSM business prior to agreeing a percentage and signing the contract. This is particularly important if a percentage of feed costs are paid by the VOSM.
- The VOSM must complete a sensitivity analysis to understand how their business can withstand different milk prices.

Skills required

The VOSM will need:

- farm management skills
- financial management/budgeting skills
- people management
- Health & Safety knowledge
- Environmental compliance and regulations for region

Financial

Drivers

The main drivers for this option are cash returns driven by the negotiated percentage share of milk income, milk production and minimising farm working costs.

Equity required

A VOSM requires minimal equity. They will typically provide labour, farm bikes and tools. At the start of the season working capital is necessary to cover wages and drawings, fuel and shed costs for the first three months until milk income starts coming in is required. This may be a significant amount for some businesses.

Financial returns

Will vary, mostly dependent on milk price.

Example of exposure to milk price:

Farm production: 150,000kg MS
VOSM income: 23% share of milk income
VOSM business expenses: equivalent to $1.20/kgMS (with 23% share of feed costs)

Low milk price:
Milk price of $3.80/kgMS x 23% = $0.87/kgMS income
Loss of $0.33/kgMS or $49,500

High milk price:
Milk price of $8.00/kgMS x 23% = $1.84/kgMS income
Profit of $0.64/kgMS or $96,000

How easy is it to enter/exit agreements

VOSM agreements are relatively simple and easy to enter and exit.

These VOSM agreements are governed by the Variable Order Sharemilking Agreements Order 2011, alterations to the agreement must not be detrimental to the sharemilker.