

MARKETING VERSUS SELLING FACT SHEET

SOUTHERN REGION

HOW CAN YOU IMPROVE YOUR GRAIN SELLING SKILLS?

One of the most important drivers of farm business profit is the price for commodities achieved each season. Farmers need a number of skills to achieve good prices, but are these skills in grain marketing or grain selling?

KEY POINTS

- ▶ Most grain producers are sellers, not marketers.
- ▶ Know your cost of production.
- ▶ Have strategies for grain selling.
- ▶ Volatility in price is good for grain selling.

Business profitability

Put simply, the equation for farm profits is:

$$\text{(Production} \times \text{Prices)} - \text{Expenses} = \text{Profit}$$

This equation implies that price received and levels of production have an equal impact on resulting profit. In reality, seasonal variability has proven to have a greater impact on profits than market variability, as indicated by recent studies in Western Australia.

A survey by PlanFarm, a farmer benchmarking service in WA, indicates that productivity variation accounted for almost all the profit variability in farmer results. Dr Ross Kingwell (Dept. of Agriculture & Food WA) communicated this difference as 70% of profit impact coming from productivity variations and 30% from market price variations. In recent times there had been a significant increase in price volatility. Both results indicate that the management of productivity clearly has a greater impact on profitability. However, good managers put significant effort into both the selling of grain and its production in order to maximise profits. But why is it easier to focus on production rather than selling?



PHOTO: P2PAGRI Pty Ltd

Does selling at harvest always give you the best price result?

The preference of most farmers to focus more on 'production' than 'price'. This could be due to recent market deregulations giving rise to more buyers and greater choice in the market, making this part of the farming business more complicated. It could also be that it is easier to see production happening in the paddock than to 'see' selling happening on the computer or phone. Whatever your preference, improved grain selling can lead to improved business performance. The key is to allocate efforts and resources, principally your time, in a balanced way.

Are we Grain Marketers or Grain Sellers?

The grains industry freely uses the phrase 'grain marketing'. This implies the need to use marketing skills to sell grain, which is not the case. Marketing implies that you

have a product that needs to be packaged in a certain way, promoted to the market and priced so it will sell. A good example of a product needing marketing in agriculture is stud rams. To be marketed, these products require:

- ▶ **Promotion** – Important information about the benefits of the product are advertised to the market, so that buyers can be attracted to purchase. So a sheep stud will advertise the benefits of the various traits being bred into its stud rams.
- ▶ **Positioning** – This is where the product sits in the market when it comes to quality and price. In the stud sheep industry, presenting rams at sheep competitions and gaining prizes greatly assists with reputation building and demonstrates quality.

- Packaging** – How is the product to be presented and packaged? Again ram sales are a good example where every effort is made to present the animal. Grooming and supplementary feeding help to present stock in excellent condition.
- People** – Often ‘word of mouth’ helps spread the reputation of a product. If you respect someone’s opinion and they say how good the product is, then you are more than likely to also purchase that product.
- Pricing** – The marketer often sets the price for the product and they may have some market power or a very good reputation. Hence, the ram from a reputable stud could sell for \$5,000/hd, where other studs may only achieve \$1,000/hd for their rams.

The marketing of stud rams requires skills that address the aspects listed above. However, when you are selling a bulk commodity like grain, you do not need to address these marketing aspects as the bulk commodity market place is different.

In selling a bulk commodity with limited ability to differentiate your product, such as grain, fruit, vegetables and minerals, prices are set by both the supply and the demand in the market place at a particular point in time. Generally, producers of these bulk commodities can only sell at the price set by the market place. There are few examples where farmers have differentiated their grain in an attempt to attract a higher price. One good example is Kangaroo Island Pure Grain, which has achieved higher canola prices exporting to Japan. Being 22km from the mainland by sea allows them to guarantee that their grain contains no genetically modified material and has been grown with minimum chemical inputs.

However, the vast majority of Australia’s grain has little differentiation for the bulk commodity market, which means farmers have no influence over the market price for their grain. While they do not influence the market, they can access higher prices on offer (over the season or even during a day) by choosing when to sell, who to sell to and what pricing mechanism to use. So sellers of bulk commodities are generally price takers.

Given this observation, grain producers are **grain sellers**, not grain marketers, and as such require different skills.

Figure 1 Variation in Australian Wheat Prices over the last decade



Source: <http://www.indexmundi.com/>

Grain market deregulation has caused fundamental change

Due to recent grain market deregulation, there has been an increase in the number of ways grain can be sold. There is now a two-year window of opportunity to sell grain via forward selling well before harvest to selling grain well after harvest out of storage. As grain prices do fluctuate widely (Figure 1), it provides grain sellers with the opportunity of taking advantage of prices when they are high and not selling when prices are low. These decisions are also made depending on the cash flow needs of the business.

Skills of a good grain seller: What strategies do farmers have to maximise profitability?

With little ability to influence the market price for their product, individual grain producers must look to other strategies to increase their farm business profitability. Consider again the equation for profit:

$$(\text{Production} \times \text{Prices}) - \text{Expenses} = \text{Profit}$$

As producers, farmers can affect their profitability at one of three points: production, costs or sale.

As **grain sellers**, what are the crucial skills needed at each of these stages?

Know how much you have to sell

This is one of the major challenges when it comes to selling grain, as farmers can now

sell grain both before and after harvest. Looking at your property’s historic grain production is a good start to making an estimate at the beginning of the season. However, actual production is very dependent on the area planted and the type of season experienced.

Know your cost of grain production

This valuable information is specific to each farming business. Refer to the ‘Cost of Production’ Fact Sheet in this series (referenced in Useful Resources) to see how to calculate the cost of production. The cost of production is also sensitive to seasonal results. A high production season will lead to a low cost of production, as there are more tonnes over which to spread the costs. The opposite occurs in a poor production season. However, it is important to know the range of your cost of production, so that when sales are made, profits are also being made.

Know the market

It is important to know the market and its price movements. Grain prices are readily available with numerous electronic services providing timely information. While it is difficult to predict both the highs and lows of the market, some guide can be gained from historic price movements as shown by the ASW Wheat Price Deciles in Table 1. This table gives an indication of both high and low prices and the deciles provide an understanding of the range of prices. For example, the Decile 5 price of \$230/t means that 50% of the last 10 years ASW wheat prices were below this level, so this

price is near average. The Decile 9 price of \$352/t means that 90% of the ASW prices in the last 10 years were below this price.

The last 10 years of market data can be used as a guide to high or low prices in the market. Obviously, it is good to sell when the market is in a high position.

**Table 1 Wheat Price Deciles
(June 2003 – June 2013)**

APW MG Wheat (\$/t)	
Highest on Record	\$420
Decile 9	\$352
Decile 8	\$309
Decile 7	\$292
Decile 6	\$256
Decile 5	\$230
Decile 4	\$212
Decile 3	\$191
Decile 2	\$170
Decile 1	\$156
Lowest on Record	\$146
Average	\$241

Source: Rural Directions P/L

Know the various opportunities you have to sell grain

One of the most significant challenges for farmers is to understand the numerous choices they have for selling grain and select the appropriate choice when the opportunity arises. Table 2 provides a broad description of the major choices available, but further research from the grain selling industry is recommended.

Effectively, farmers can be selling wheat and other grains from about 12 months before harvest to 12 months after harvest, which means there are approximately two years of price movements from which to choose grain prices that suit the production profile of the business. The challenge is in having the nerve to balance the prices with the ability to deliver.

Know the risks

Price risk management is where the risk of price variations is managed using the range of wheat selling choices available, as listed above. However, some of the greatest risks

Table 2 Choices for Selling Grain

Forward selling	<ul style="list-style-type: none"> • Physical contracts - This could be a physical forward sale where a contract for the amount of grain and price are agreed. The grain is then delivered at harvest to fulfil the contract. There is a risk that more production is contracted than is actually produced. • Swaps - In the grain futures market, either futures contracts or options are used to secure a price well before harvest. Most major banks provide these services and they are called swaps. This type of market instrument works like a form of insurance for prices, as the grain is still delivered to the local authorities. Contact your bank for more information.
At harvest	<ul style="list-style-type: none"> • Cash - Sell grain for cash to brokers at harvest. • Grain pools - Sell to an industry grain pool where the pooled grain is sold over a period of time and the average prices are returned to the producer. This will have cash flow ramifications, as grain pools take some months before all payments are made.
After harvest	<ul style="list-style-type: none"> • Store in the industry silo system - Deliver the grain to the silo system and sell the grain sometime after harvest. This option for grain storage is generally available for 8 months after delivery. • Store on-farm - Store the grain on farm in storage infrastructure owned by the farm. This grain can be sold later and there is no time limit for storage, although the responsibility to maintain grain quality rests with the farmer.

can come from not fully understanding how some of these grain selling choices operate. For example when a large number of farmers started using forward contracts a few years ago - the dry spring greatly reduced their production and they found themselves short of the tonnes needed to fulfil their contracts. At the same time, the grain price rose and so going out at harvest and buying the necessary grain to fulfil their contract shortfall cost them additional money for which they had not budgeted. This cost some grain farmers the significant amount of over \$100,000; when they thought they were managing their risk, they actually increased it.

Risks associated with grain selling include:

- **Solvency** - Solvency means how viable is the grain trader or broker you are dealing with. There are still grain brokers going into liquidation leaving farmers with significant losses from unpaid grain payments. To gain some understanding of a grain trader's credit rating, contact your bank or local farmer organisations for information.
- **Contract risk** - When you enter into a contract at any time, you need to understand your obligation if things go wrong, as a contract is a legal

document. This could include your inability to supply both the quality and quantity of grain due to seasonal challenges. You need to know who is liable for this and if there is any account taken of the season.

Some farmers pay grain selling advisers to assist with their grain selling, as this can be a technical area requiring specific knowledge.

Set a strategy for selling

It is a good idea to have a grain selling plan, to separate the emotion from the logic of making a decision. Some of the strategies available to farmers include:

- Chase the market and aim to sell at the highest price - an expert can be hired to assist with keeping an eye on both the current and future markets, and advise when it is best to sell. The challenge here is that even the experts find it difficult to predict market price shifts as these could be influenced by unpredictable adverse weather conditions such as flood, fire and poor rainfall in other grain producing countries.
- Sell for cash at harvest only - All the grain is to be sold at harvest right off the header, as it is only then that the

total production is known. Sometimes harvest prices can be good or poor. This strategy means you are at the mercy of the market at harvest.

- Sell to grain pools only – Traditionally, most farmers used grain pools, especially when the Australian Wheat Board (AWB) had the ability to trade forward grain prices. This form of selling resulted in prices being averaged over a period of time. Grain pools in the current market do not have the old AWB advantage of forward selling, so tend not to perform as well. This form of selling means growers need to be happy that full payment may not be received for some months.
- Sell 33%:33%:33% - This is where a third of the crop is sold using forward selling methods, a third is sold for cash at harvest, and a third is stored and sold some time after harvest. This is another form of averaging, allowing the grower to be more in control of the timing of grain sales, and to hopefully achieve 'higher than average' prices.
- Sell 50%:50% - Similar to method above, except 50% is sold at various times prior to harvest and 50% is stored to be sold at various times after harvest. No cash sales are made at harvest, as it is a busy period on the farm and this is the time of the year that most of Australia's grain gets sold, so prices may not be the best. This is another attempt at achieving results higher than the industry average.
- Any variation or combination of the above strategies.

FAQs

How do I know if the grain broker I use is good?

The answer to this question lies in the quality of service and trust. Also, you need to be clear as to what services you require. For example, this may include regular market up-dates, personal and understandable commentary of what is affecting the market and what is expected in the future, and/or someone who understands the risks of selling and can

advise on the best strategies. Once you have this list, a good source of information comes from other farmers' experiences, so ring around and do your research.

Is using a grain broker worth the investment?

This is a difficult question as it requires you to estimate what grain net income you would have achieved using your own grain selling skills versus what may be achieved using professional advice and then compare the results. The difficulty is that you will not know this before the season and it takes discipline to record what you would have done without the professional as the season unfolds.

Another test is to ask yourself whether you are going to put in the effort needed to study the market throughout the year and to know what each selling choice is offering as the season unfolds. If you are not willing to put in the necessary time, then perhaps professional advice will provide you with additional income to cover its cost.

Is there one marketing plan that stands out better than others?

You would think one particular plan would work best as the international market lives with the northern and southern hemispheres seasonal harvest cycles. However, this is interrupted by significant world climate events that affect this production cycle. So a plan that is good one year may not be the best the following year. The best marketing plan is to aim to achieve an 'above average' price by using both marketing information and observing the prices being offered by the range of choices available and comparing this to your cost of production. It is a bit like playing cards, as you know the rules and need to play each season on its merits.

Are there rewards for improving your knowledge of grain selling?

Again, this is difficult to answer but it largely depends on how much time and effort you are willing to put in to understanding all the sell choices, selecting a plan and then having the discipline to implement the plan. Farmers who have put in this effort have reported significantly improved profits, but

it depends largely on the desires of each individual farmer.

USEFUL RESOURCES

Related GRDC Fact Sheets

Other fact sheets in this Farm Business Management series provide further detail on farm financial tools:

- Farm Business Overview (Order Code: GRDC909),
- Cost of Production (Order Code: GRDC912),
- Farm Business Costs (Order Code: GRDC935),
- Production Economics (Order Code: GRDC937) and
- Key Financial Ratios (Order Code: GRDC911).

Copies of the above fact sheets are FREE plus P&H and available from:

Ground Cover Direct Freephone: 1800 11 00 44 or email: ground-cover-direct@canprint.com.au

These can also be downloaded from www.grdc.com.au/fbm

Plan to Profit (P2P), a whole-farm financial management program – this will assist with calculating a farm's financial budgets: Cash Flow, Profit and Loss, Balance Sheet and Gross Margins.

www.P2PAgri.com.au

MORE INFORMATION

Mike Krause

P2PAgri Pty Ltd
08 8396 7122
www.P2PAgri.com.au



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