NORTHERN
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GROWNOTES™

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GRAINS RESEARCH & DEVELOPMENT CORPORATION

VETCH

SECTION 15

MARKETING

PRICE DETERMINANTS FOR FEED GRAINS IN NORTHERN MARKETS | EXECUTING TONNES INTO CASH | ENSURING ACCESS TO MARKETS FOR NORTHERN AUSTRALIAN FEED GRAINS

Marketing

The final step in generating farm income is converting the tonnes produced into dollars at the farm gate. This section provides best in class marketing guidelines for managing price variability to protect income and cash-flow.

15.1 Price determinants for feed grains in northern markets.

Stock feed markets are the biggest consumers of grain domestically in Australia.

Domestic stock feed grain consumption in Northern Australia is equivalent to approximately 45% of the total winter crop produced in NSW and Qld. Furthermore the domestic market in Victoria traditionally will draw grain in from NSW to support domestic stock feed markets as well as bulk and container export programs. Further drawing on stocks in Northern markets.

The biggest stock feed market in northern Australia is the beef industry representing 45% of all stock feed demand in these markets, followed by the poultry industry at 30%.

Whilst the poultry industry remains a strong source of demand for feed grains in northern markets intensive livestock industries such as poultry and pig meat continue to experience geographic relocation. Whilst to some extend Qld has been able to benefit from a shift in pig meat production away from NSW, the stronger trend across both these industries is a move away from East Coast markets to South Australia and Western Australia.

This geographic shift is being driven by the availability of land, of feed grains and a more favourable regulatory environment.

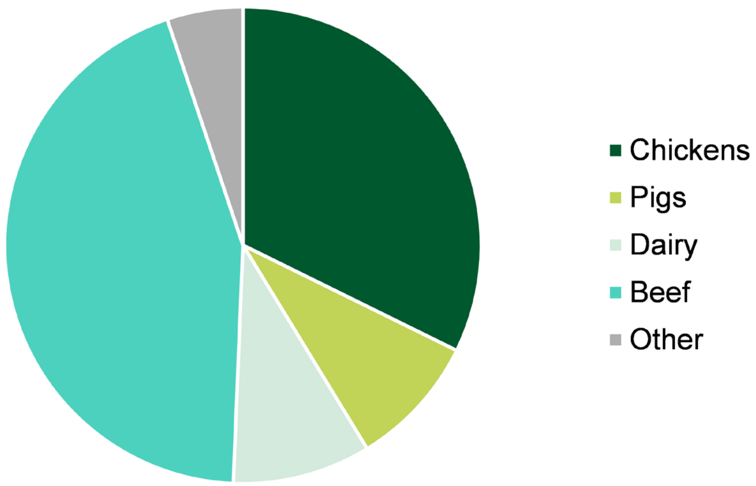


Figure 1: *Sources of demand for stock feed in Northern Australia*

The key drivers of prices for feed grains in Northern markets include;

- Rate of exports and remaining supply of feed grains for domestic markets.
- Commodity prices in the consuming industry (ie meat prices – especially for beef)
- Consumption trends in domestic livestock markets.
- Livestock health
- Seasonality / supply of pasture and fodder vs grains.

- Imports of alternate feed sources (ie soy bean meal)
- Prices of competing feed grains.
- Regulatory changes

15.2 Executing tonnes into cash

When it comes to accessing domestic stock feed markets there are several ways this can be approached.

1. Sale to a feed miller or manufacturer
2. Sale direct to farm or end user.
3. Sale to a trader or merchant who on sells this grain to the stockfeed market.

Each organisation will differ in terms of how they manage grain purchases, the professionalism of the enterprise and management around grain requirements and grain purchases, documentation and record keeping.

Hence it is particularly prudent when making sales into these markets to be vigilant in maintaining records of contracts, even when they are executed by phone. It is strongly advised that the seller keeps a written record of the particulars of the contract including price, quantity, quality, delivery and payment terms to protect yourself in the event of a dispute with your counterparty as to the details of the sale agreement.

It is even better practice to send a contract confirmation to the buyer in the event they don't provide one to you, or even as well as. Grain Trade Australia provide standard form contract documents which can be completed by either party and returned to the buyer by email as confirmation of the verbal contract. This way, any mis-understandings that may have taken place on the phone can be quickly identified and rectified immediately whilst the conversation is still fresh in both your minds rather than waiting until delivery to identify a problem.

15.2.1 How to sell for cash

Like any market transaction, a Cash grain transaction occurs when a bid by the buyer is matched by an offer from the seller. Cash contracts are made up of the following components with each component requiring a level of risk management:

Price

Future price is largely unpredictable hence devising a selling plan to put current prices into the context of the farm business is critical to manage price risk.

Quantity and Quality

When entering a cash contract you are committing to delivery of the nominated amount of grain at the quality specified. Hence production and quality risk must be managed.

Delivery terms

Timing of title transfer from the grower to the buyer is agreed at time of contracting. If this requires delivery direct to end users it relies on prudent execution management to ensure delivery within the contracted period.

Payment terms

In Australia the traditional method of contracting requires title of grain to be transferred ahead of payment; hence counterparty risk must be managed.

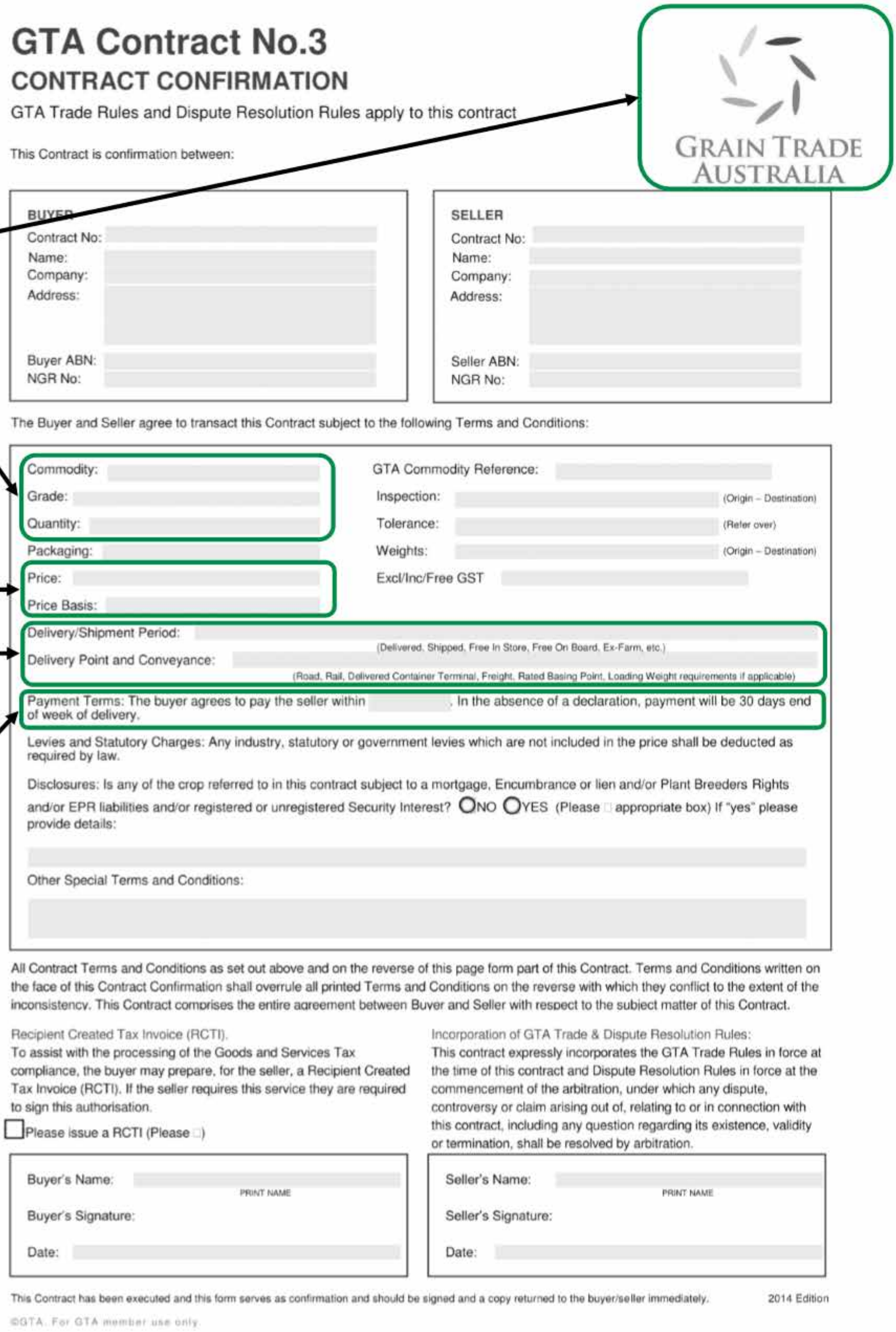
Grain Trade Australia is the industry body ensuring the efficient facilitation of commercial activities across the grain supply chain. This includes contract trade and dispute resolution rules. All wheat contracts in Australia should refer to GTA trade and dispute resolution rules.

Quantity (tonnage) and quality (bin grade) determine the actuals of your commitment. Production and execution risk must be managed.

Price is negotiable at time of contracting.
Price basis or price point is important as it determines where in the supply chain the transaction will occur and so what costs will come out of the price before the growers net return.

Timing of delivery (title transfer) is agreed upon at time of contracting. Hence growers negotiate execution and storage risk they may have to manage.

Whilst the majority of transactions are on the premise that title of grain is transferred ahead of payment this is negotiable. Managing counterparty risk is critical.



GTA Contract No.3

CONTRACT CONFIRMATION

GTA Trade Rules and Dispute Resolution Rules apply to this contract

GRAIN TRADE AUSTRALIA

This Contract is confirmation between:

BUYER
Contract No:
Name:
Company:
Address:
Buyer ABN:
NGR No:

SELLER
Contract No:
Name:
Company:
Address:
Seller ABN:
NGR No:

The Buyer and Seller agree to transact this Contract subject to the following Terms and Conditions:

Commodity:
Grade:
Quantity:
Packaging:
Price:
Price Basis:

GTA Commodity Reference:
Inspection: (Origin – Destination)
Tolerance: (Refer over)
Weights: (Origin – Destination)
Excl/Inc/Free GST

Delivery/Shipment Period:
(Delivered, Shipped, Free In Store, Free On Board, Ex-Farm, etc.)
Delivery Point and Conveyance:
(Road, Rail, Delivered Container Terminal, Freight, Rated Basing Point, Loading Weight requirements if applicable)

Payment Terms: The buyer agrees to pay the seller within . In the absence of a declaration, payment will be 30 days end of week of delivery.

Levies and Statutory Charges: Any industry, statutory or government levies which are not included in the price shall be deducted as required by law.

Disclosures: Is any of the crop referred to in this contract subject to a mortgage, Encumbrance or lien and/or Plant Breeders Rights and/or EPR liabilities and/or registered or unregistered Security Interest? ◯NO ◯YES (Please ☐ appropriate box) If "yes" please provide details:

Other Special Terms and Conditions:

All Contract Terms and Conditions as set out above and on the reverse of this page form part of this Contract. Terms and Conditions written on the face of this Contract Confirmation shall overrule all printed Terms and Conditions on the reverse with which they conflict to the extent of the inconsistency. This Contract comprises the entire agreement between Buyer and Seller with respect to the subject matter of this Contract.

Recipient Created Tax Invoice (RCTI).
To assist with the processing of the Goods and Services Tax compliance, the buyer may prepare, for the seller, a Recipient Created Tax Invoice (RCTI). If the seller requires this service they are required to sign this authorisation.

☐ Please issue a RCTI (Please ☐)

Incorporation of GTA Trade & Dispute Resolution Rules:
This contract expressly incorporates the GTA Trade Rules in force at the time of this contract and Dispute Resolution Rules in force at the commencement of the arbitration, under which any dispute, controversy or claim arising out of, relating to or in connection with this contract, including any question regarding its existence, validity or termination, shall be resolved by arbitration.

Buyer's Name: PRINT NAME
Buyer's Signature:
Date:

Seller's Name: PRINT NAME
Seller's Signature:
Date:

This Contract has been executed and this form serves as confirmation and should be signed and a copy returned to the buyer/seller immediately. 2014 Edition

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Figure 2: *Typical cash contracting as per Grain Trade Australia standards.*

15.2.2 Counterparty risk

Most sales involve transferring title of grain prior to being paid. The risk of a counterparty defaulting when selling grain is very real and must be managed. Conducting business in a commercial and professional manner minimises this risk.

Principle: "Seller beware" – There is not much point selling for an extra $5/t if you don't get paid.

Counterparty risk management includes:

1. Dealing only with known and trusted counterparties.
2. Conduct a credit check (banks will do this) before dealing with a buyer they are unsure of.
3. Only sell a small amount of grain to unknown counterparties.
4. Consider credit insurance or letter of credit from the buyer.
5. Never deliver a second load of grain if payment has not been received for the first.

If possible, do not part with title of grain before payment or request a cash deposit of part of the value ahead of delivery. Payment terms are negotiable at time of contracting,

Above all, act commercially to ensure the time invested in a selling strategy is not wasted by poor counterparty risk management. Achieving $5/t more and not getting paid is a disastrous outcome.

15.2.3 Read market signals

The appetite of buyers to buy a particular commodity will differ over time depending on market circumstances. Ideally growers should aim to sell their commodity when buyer appetite is strong and stand aside from the market when buyers are not that interested in buying the commodity.

Principle: "Sell when there is buyer appetite" – When buyers are chasing grain, growers have more market power to demand a price when selling.

Buyer appetite can be monitored by:

1. The number of buyers at or near the best bid in a public bid line-up. If there are many buyers, it could indicate buyer appetite is strong. However if there is one buyer $5/t above the next best bid, it may mean cash prices are susceptible to falling $5/t if that buyer satisfies their buying appetite.
2. Monitoring actual trades against public indicative bids. When trades are occurring above indicative public bids it may indicate strong appetite from merchants and the ability for growers to offer their grain at price premiums to public bids.

15.2.4 Know the specifications of your grain

Feed 'grades' of grain as defined by bulk handler receival standards can have very broad quality specifications. For the lowest grades there is often no minimum tolerances on screenings or protein hence no two parcels are the same.

The important factor for the stock feed market however is not what 'grade' the grain is but its energy and protein components which ultimately determine conversion in to meat or other animal products. Hence by having your grain tested and knowing your specifications helps the buyer to know exactly what the value of the grain will be in the production system.

Without this information the buyer may base their pricing on the 'minimum' specification or likely worst case scenario, to protect themselves in the event they receive grain of the lowest quality allowable in the grade specifications. However knowing why your grain was downgraded and the specifications of the load, the buyer may be able to pay premiums for the exact quality you are offering, above the minimum specification.

15.3 Ensuring access to markets for Northern Australian feed grains

Planning on where to store the commodity is important in ensuring access to the market that is likely to yield the highest return.

Animal industries such as pigs and poultry are highly intensive and tend to be geographically concentrated. Hence proximity to these markets can be an important determinant of market access. Some growers may not have access to these markets at all due to large distances between production and demand making the cost of transport prohibitive to profitably accessing these markets.

In Northern Australia some of the largest delivered markets include Brisbane (Qld), Darling Downs (Qld), Texas / North Star (NSW), Riverina (NSW). Hence once again proximity to these markets must be considered as party of any marketing plan to access demand from the stock feed industry.

15.3.1 Storage and Logistics

Return on investment from grain handling and storage expenses is optimised when storage is considered in light of market access to maximise returns as well as harvest logistics.

Storage alternatives include variations around the bulk handling system, private off farm storage, and on-farm storage. Delivery and quality management are key considerations in deciding where to store your commodity.

Commodities destined for the domestic end user market, (e.g feed lot, processor, or container packer), may be more suited to on-farm or private storage to increase delivery flexibility.

Storing commodities on-farm requires prudent quality management to ensure delivery at agreed specifications and can expose the business to high risk if this aspect is not well planned. Penalties for out-of-specification grain on arrival at a buyer's weighbridge can be expensive. The buyer has no obligation to accept delivery of an out-of-specification load. This means the grower may have to incur the cost of taking the load elsewhere whilst also potentially finding a new buyer. Hence there is potential for a distressed sale which can be costly.

On-farm storage also requires prudent delivery management to ensure commodities are received by the buyer on time with appropriate weighbridge and sampling tickets.

Principle: "Storage is all about market access" – Storage decisions depend on quality management and expected markets.

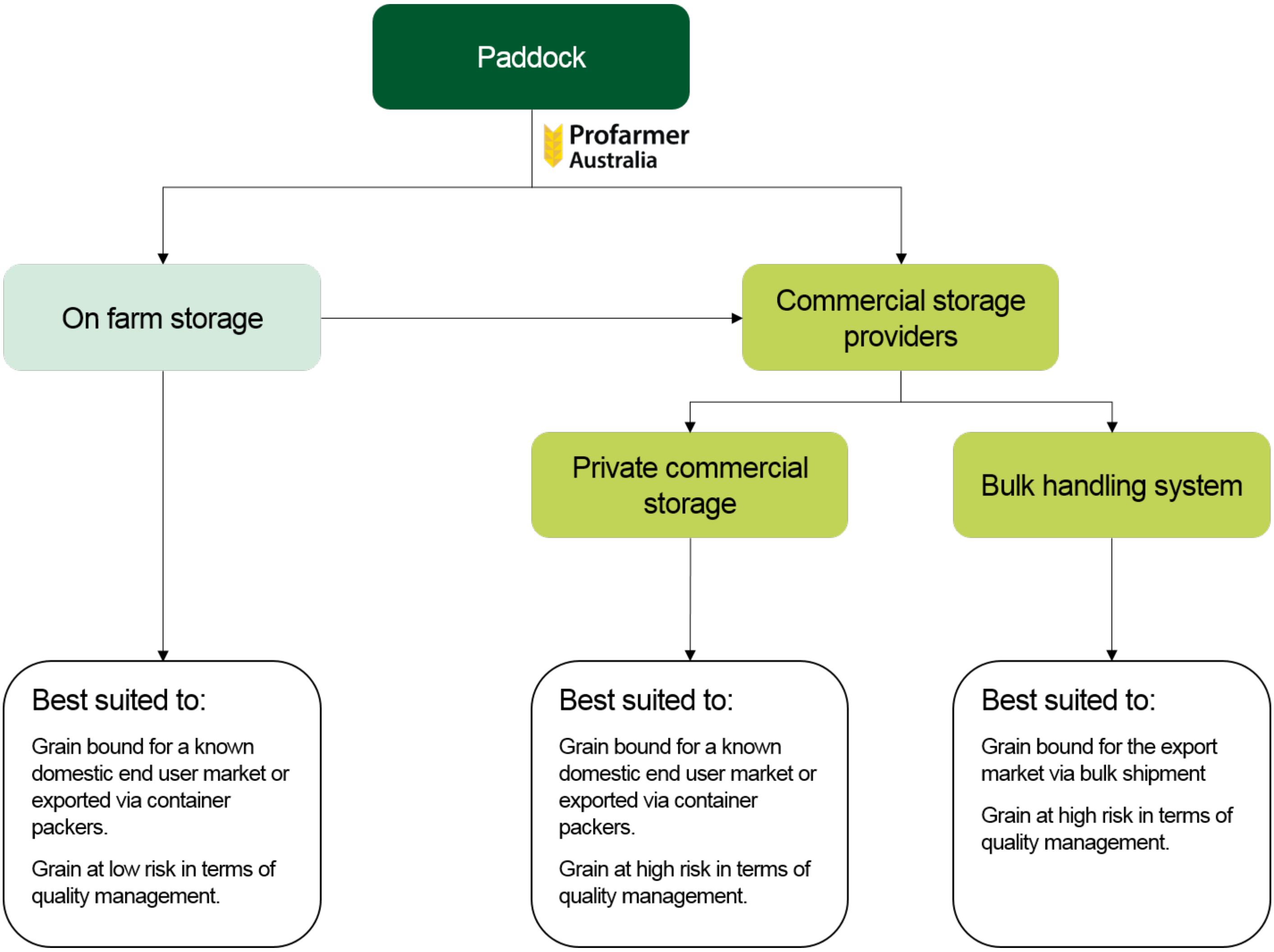

Figure 3: *Grain storage decision making*

Decisions around storage alternatives of harvested commodities depend on market access and quality management requirements.

15.3.2 Separate the delivery decision from the pricing decision

Organised stock feed buyers, with a clear out look as to what their grain requirements will be across the season may seek to purchase their grain in advance of delivery. That is they may purchase grain in March for delivery between May and July. This provides the seller the opportunity to obtain price certainty immediately whilst delivery may not take place until some point in the future.

The benefit of this is that a seller can capture strong value when it presents, even though it may not be a convenient time to arrange delivery. Or you can create cash flow certainty for a known future commitment at today's price.

15.3.3 Cost of carrying grain

Storing grain to access sales opportunities post-harvest invokes a cost to "carry" grain. Price targets for carried grain need to account for the cost of carry.

Carry costs for canola are typically $4-5/t per month consisting of:

1. monthly storage fee charged by a commercial provider (typically ~$1.50-2.00/t per month)

2. the interest associated with having wealth tied up in grain rather than cash or against debt (~$2.50-$3.00/t per month depending on the price of the commodity and interest rates.

The price of carried grain therefore needs to be $4-5/t per month higher than what was offered at harvest.

The cost of carry applies to storing grain on farm as there is a cost of capital invested in the farm storage plus the interest component. $4-5/t per month is a reasonable assumption for on farm storage.

Principle: “Carrying grain is not free” – The cost of carrying grain needs to be accounted for if holding grain and selling it after harvest is part of the selling strategy.

Principles revised

“Always keep written records” – thorough record keeping is everyone’s responsibility not just the buyers.

“Seller beware” – Know your counterparty

“Know your specs” – grades don’t always convey quality

“Separate the delivery decision from the pricing decision”

“Sell when there is buyer appetite” – When buyers are chasing grain, growers have more market power to demand a price when selling.

“Storage is all about market access” – Storage decisions depend on quality management and expected markets.

“Carrying grain is not free” – The cost of carrying grain needs to be accounted for if holding grain and selling it after harvest is part of the selling strategy.