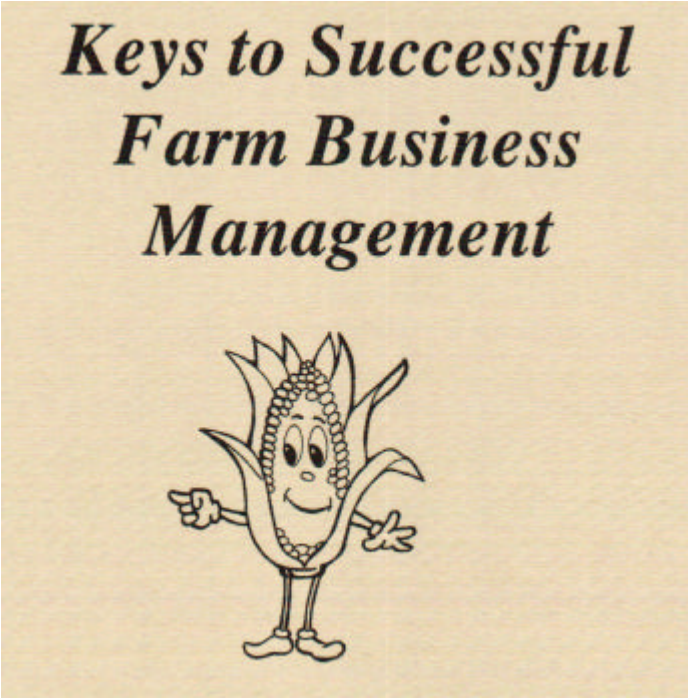

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Developing and Implementing a Successful Marketing Plan

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Key Points

* Find reliable sources of marketing information, and learn how to use them.

* Understand that there are a variety of acceptable ways to respond to price risks.

* Develop your own strategy for marketing.

* Keep your plan simple and consistent, and base it on all available facts about market conditions.

* Learn to follow a basic list of rules when making marketing decisions.

Introduction

Although your marketing attitude affects how you view the market, market profitability can be increased by improving your marketing skills. Developing a sound marketing plan that works for you is the first step to improving profitability. Learning alternative pricing methods is an important part of this process, but also being aware of some basic marketing principles and following specific rules will help as you develop your marketing strategy.

As you develop your marketing plan, remember that marketing is an integral part of your entire business. It is not a separate component. Your marketing decisions will affect the rest of the business. Therefore, you need to understand what the impact of various marketing decisions will be before you make them.

Find reliable sources of marketing information, and learn how to use them.

Obtaining marketing information is a useful way to begin planning for marketing decisions. With the advent of market data telecommunication systems, up-to-date market information is easily accessible in most rural areas. Knowing market conditions makes it possible to make informed decisions before buying or selling crops and livestock. Recording trends in the market allows farmers who watch the market to gain additional confidence in making critical buy/sell decisions. A thorough understanding of government programs is also advantageous for the farmer seeking to realize the greatest profit margin.

Understand that there are a variety of acceptable ways to respond to price risks.

There are several alternative pricing methods available to help reduce price variability and/or protect profitable production levels. These can be considered marketing tools. When making marketing decisions, you can take advantage of a variety of pricing alternatives in order to increase and protect the profitability of your farm business.

For example, in lieu of selling a crop at harvest, which can sometimes mean taking a poor price, alternative pricing methods such as *spreading crop sales* over the calendar year allow you the flexibility to wait for prices to increase. Although other factors such as storage costs and the overall world market outlook should be considered when planning crop sales, the commodity market gives the farm manager a wide choice of selling alternatives.

Another alternative pricing method is *forward contracting*. Forward contracting is promising to sell one's crops at a future date at a specific price for the purpose of guaranteeing a specific level of profit.

Hedging is another available marketing tool. Hedging is simply utilizing a futures position that is equal (in quantity) and opposite (in position) to an already existing cash position. Hedging tends to give the producer more flexibility when compared to forward contracting, but it does involve additional costs such as commission and interest on margin money. A hedger is a producer who uses the future market to help manage risk and protect profits.

Since 1984, *options* have been available to agricultural producers as a pricing alternative. Options facilitate the transfer of price risk to others. Agricultural options provide a type of price insurance to producers. An option gives the buyer the right, but not the obligation, to buy or sell a commodity at a specified price during a specified period of time. Options must have a writer, that is, someone who assumes the risk in exchange for a premium paid. This premium is a market-determined price set on the exchange floor by options buyers and sellers. Options are exercised at the buyer's discretion. The seller is obligated to provide the future position when the option is exercised. A *put option* is the right to sell the underlying futures contract, while a *call option* represent the right to buy the underlying futures contract.

Case in Point

When Jake Peters heard that his neighbor was going to retire, he talked to him about buying the 80 acres that bordered the Peters farm. The neighbor, Francis Smith, was glad to learn of Jake's interest, but he knew that his 80 acres would be easy to sell.

Jake explained to Francis that he needed time to talk to his family and banker, but thought the asking price of $1500 per acre was fair. Francis offered to sell Jake an option to buy the 80 acres for $20 an acre. The offer would be good for 90 days. Jake agreed and wrote Francis a check for $1600. Spending $1600 was well worth it for Jake to buy the assurance that he had 90 days to secure financing to buy his neighbor's 80 acres at the $1500 per acre price.

If Jake failed to get financing, it would mean not being able to purchase the 80 acres and he would lose his $1600. On the other hand, if Jake did receive financing from the bank, he would purchase the 80 acres. The important point is that for the next 90 days Jake had control over what happened to the acreage. The $1600, like an insurance premium paid, protected the land for Jake. In accepting the payment, Francis could not sell the land to anyone else for 90 days, regardless of what they might be willing to pay.

This transaction is actually similar to a call option, giving the purchaser the right to buy a specific commodity before the expiration date. The important criteria in this example include an option writer (Francis Smith), an option buyer (Jake Peters), an underlying commodity (80 acres), a strike price ($1500 per acre), an option maturity (90 days), and an option premium ($1600).

The other type of option is the put option. Many agricultural producers choose to use the put option because it gives the purchaser the right to sell the underlying futures contract at the strike price any time before the option's expiration date.

Develop your own strategy for marketing.

Once you have an understanding of what basic marketing tools are available, planning a strategy for your own marketing plan is the next step to success in the market. Following a consistent market strategy will help you make pricing decisions.

The strategy that is put into action must not only demonstrate consistency but must also reflect your overall marketing attitude. A successful farm business manager is always looking at and ready to accept new alternatives, but acts cautiously. An uncertain outlook should never be a reason for inaction. With a consistent marketing plan, you can follow the daily market and be prepared to make marketing decisions. It is important to remember that inaction is as much a decision as any action.

Keep your overall plan simple and consistent, and base it on facts about market conditions.

If you keep your marketing plan simple, the emotion and stress associated with it will also be kept to a minimum. A workable marketing plan allows you to look at market information, but never to overuse the news. The emotions of greed, hope, or fear should not control market actions. The prospect of an extra half cent shouldn't lure you away from a planned, consistent approach to marketing. Experts cannot outguess the market; individual farmers should not try.

A sound marketing plan is based on available, known information and not on the unknown future. Not being able to predict future commodity or livestock prices and conditions should not be a reason for inaction. Marketing projections should be based on the pertinent information that is available. All available pertinent information should be considered with regard to your own marketing mentality before making marketing decisions. Perhaps we could compare the process to the simpler buying and selling evaluation that occurs whenever goods are exchanged. It is always wise to consider all known facts when making financial decisions.

Case In Point

When Farmer Holt decided to sell his 1982 Oldsmobile 98, he made a list of the important facts about the car for interested buyers. He stated that the car gets 15 miles per gallon and averages $1500 in repair expenses annually. He included in the fact sheet that the car had 100,000 miles to its credit. It costs $35 annually to license the car, and insurance is $220 annually. He did not list how much he wanted for the car. Mr. Holt posted the information about the car at the local coffee shop.

It wasn't long before his neighbor called to say he was interested in buying the 1982 Oldsmobile. The neighbor asked Mr. Holt how much he wanted for the car. Mr. Holt replied, "What do you think would be a reasonable offer?" The neighbor answered, "Well, how should I know what your car is worth?" Mr. Holt answered, "In that case, I would like $24,000 for my car." When the neighbor gasped at that figure, Mr. Holt said, "I gave you some pertinent facts about the car and thought you'd be able to figure a reasonable price for the car on that basis. If you cannot, then I'll just try to get as much as I can for it!"

The potential buyer in the example did not consider the available facts when proclaiming not to know the car's worth. Although farmers will never be able to predict the marketing outlook completely, the challenge in marketing is to be able to make reasonable projections based on the known facts. The prudent and reasonable farmer who makes marketing decisions based on available information decreases vulnerability to loss by knowing as much as possible about market conditions.

Utilizing commodity price charts and learning to evaluate trends when making market projections is an important part of any market research. Likewise, production and stock reports and information on weather and other conditions affecting production variation are important fundamental factors which are

critical considerations in marketing decision making.

Learn to follow a basic list of rules when making marketing decisions.

Almost all professional traders adhere to a set of "rules" which govern how they trade the markets. These rules are based on their marketing principles. When trading, producers should know the mechanics of the markets and attempt to develop their own set of rules. Basically, your rules should serve as a guide that will help you make trading more objective and less subjective. The following marketing recommendations are presented to assist you in developing a workable set of rules.

First, know why you're using the markets. Your purpose as a producer, or hedger, is to hold grain and sell futures in an attempt to shift the risk of price level fluctuation to someone else. Speculators, on the other hand, take a market position to make money based upon some fundamental (supply-demand) or technical (price charts) information. As a producer, do not confuse your position with that of a speculator. Remember that you are a producer and that the position you take in the market should reflect your purpose and be a part of your overall marketing plan.

Second, always trade with the trend. Although this is probably more appropriate for speculators, hedgers who read price charts and see an obvious strong uptrend in the market may want to delay their short, or sell futures, position in the market. Remember, one shouldn't attempt to outguess the market.

The third recommendation is do not play wait and see. If your marketing plan has set some price objective and it is reached--take action. Just because the market was up yesterday and again today, doesn't mean it will be up tomorrow. Producers who continually try to get that extra cent or two out of the market before they sell are usually disappointed with the outcome of their marketing efforts.

Consideration number four suggests the use of stops. This is probably more appropriate for those in a speculative position, although if you sell grain in the fall and are long futures, a speculative position, you should seriously consider setting stops to get you out of the market if it turns quickly. Stops can also be changed as the market goes in your favor to give you a profit when the market goes the other way.

The fifth recommendation suggests you take your losses. Another way of stating this is "don't meet margin calls." This axiom is for speculators only. As a hedger, a loss in the futures side of your trade means that the cash commodity has increased in value. Your futures position as a hedger is dictated by what you do in the cash market--not the other way!

Number six reminds you to have a good reason for trading. Some people trade for the fun of it. Some people seem to trade for masochistic pleasure! You should trade because your market plan dictates a particular market action. Leave the bragging about "how I got rich in the belly market" to the speculators.

The seventh recommendation warns never to attempt to outguess the top or bottom of a market. This rule raises some of the points made in recommendation number three. Chart formations based on historical market performance (which marketing experts often use to formulate predictions) can be misleading from time to time. It may look like beans are reaching high, but new market information (supply-demand data or technical information) may quickly move the market in another direction. Again, the backbone of your trading actions should be what you've outlined in the market plan.

The eighth consideration advises placing orders at the market. There are a variety of orders with many different contingencies which can be used to enter the market. Sometimes if you are too particular about

the initial order price, the order may not be filled, the market may move a great deal, and you end up not having the position you want. Thus, enter a market order which must be filled as soon as possible at the best possible price.

The ninth market suggestion warns not to buy because the market seems too low or sell because the market seems too high. Don't be tempted to trade because you read an article about how a commodity should be priced. If the information is in the newspaper, chances are it has already been taken into account by the market. Trade because you like this price, it is profitable, and agrees with the points of your market plan.

Recommendation number ten advises never cancel a stop to avoid closing a position. You do not have the ability to immediately assess all new market information and how it may affect market price. Thus, when trading you should set stops, admit defeat when your stops are hit, and get out of the market.

As you think about these rules, remember most involve a fair amount of common sense. Certainly there are some exceptions to these rules, but, on the whole, they are relatively good advice. Many of the comments made reflect our bias that producers need to develop a marketing plan and utilize that plan to guide all their marketing efforts. Such a plan should fit your particular needs and reflect an attempt to maximize your flexibility by utilizing available marketing information and marketing tools.

Conclusion

Whatever your marketing strategy is, you will want to maximize profits and, at the same time, minimize risks. The way to balance these two goals is to tailor your marketing plan to fit your particular need. Remember also to maximize your flexibility by using available marketing tools and information.

Key Reminders

The following reminders will help you develop and implement a successful marketing plan.

1. Find one or two reliable sources of market information that you understand, and learn how to use them.

2. Learn what different types of pricing alternatives are available through the commodity market.

3. Be aware that your marketing plan must be consistent with your marketing attitude.

4. Although your plan should be simple and consistent, be flexible about considering new ideas for marketing.

5. Choose a set of rules or guidelines to follow that seem to you to be based on common sense. Consistently follow those rules when making marketing decisions.

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