Develop a Marketing Plan and Then Implement it

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Take time to develop a marketing plan for each crop that will be produced in 1999. Doing so could mean the difference between profit and loss for the farm. It could even mean the difference between survival and bankruptcy. Developing a marketing plan is probably the single most important management activity on the farm: a marketing plan for each crop is essential to overall farm financial planning. In financial planning, it is necessary to combine crop production costs (economic and cash) and government farm program payments with a marketing plan. This permits costs and returns to be estimated for the farm. Then it can be determined if the farm's cash will flow and if production will be profitable. If cash flow or profit problems appear, costs may need to be reduced or alternative enterprises considered.

It is best to keep the marketing plan for a crop fairly simple. That way it can be committed to memory and the producer will be more likely to act on it when key elements are triggered. Key elements include price objectives and time deadlines.

Price objectives are matched with time deadlines. About five objectives and corresponding deadlines are usually specified in a marketing plan. A percentage of the crop is sold when either the first price objective or time deadline is reached, another percentage of the crop is sold when either the second price objective or second time deadline is reached, and so on. The largest percentage is sold in the middle of the price range.

Time deadlines for selling a crop can be derived from the seasonal price pattern for that crop. Those times of the year when cash prices are usually the highest would be picked as selling deadlines, recognizing that they may need to be modified to meet cash flow needs and storage limitations. Seasonal price patterns for many of the crops produced in North Dakota are presented in North Dakota State University Extension Service Circular EC-921. Other universities would have similar publications for their state.

Price objectives are set relative to a goal. A goal could be to sell in the upper one-third of the price range for the marketing year. A more modest goal would be sell the crop for a price above the state seasonal average farm price. Although seemingly modest, this goal is difficult to achieve, according to marketing publications.

The seasonal average farm price expected for a crop can be derived from several sources of information. Sources include current cash prices, cash forward contract prices, the futures market, USDA's price projections and estimates by marketing advisory services.

If the goal is to sell above the state seasonal average, the lowest price objective could be set at about that level. The other price objectives could be evenly spaced so that the highest is about 115-120 percent of the lowest. Price charts can also be used as a guide in setting these other price objectives. An alternative is to set price objectives so that, on average, the seasonal average is exceeded.

An example marketing plan for 14 percent protein hard red spring wheat produced in 1999 is presented here.

Expected Production Percent	Deadline	MGE Sept. Futures Price
10	4/28/99	3.80
25	5/12/99	3.95
30	11/17/99	4.10
25	1/26/00	4.25
10	4/27/00	4.40

This plan calls for selling 10 percent of the anticipated spring wheat crop by April 28 or when the September futures price on the Minneapolis Grain Exchange reaches $3.80, whichever comes first. It calls for selling an additional 25 percent by May 12 or when the price reaches $3.95, selling an additional 30 percent by November 17 or when the price reaches $4.10, selling an additional 25 percent by January 26 of the following year or when the price reaches $4.25, and selling the final 10 percent by April 27 of the following year or when the price reaches $4.40.

A common problem for many producers is to ignore the time deadlines for selling when prices fail to reach stated objectives, a serious blow to the finances and credibility of the farm manager. Even if price objectives have been set unrealistically high, relative to outlook information, the time

deadlines make the plan realistic. Since the time deadlines are based on a recognized marketing concept (seasonal price pattern), the plan is acceptable to professional farm managers and those working with them. Producers can feel that they have made a good decision, even when price objectives are not reached.

Marketing plans need to be reviewed and adjusted as new information becomes available. USDA reports generally provide the basic information for updating. This information can be supplemented by news reports of crop conditions throughout the world, weather reports and so on.

A marketing plan can be implemented using a number of marketing tools. The best tool to use depends on the situation. The use of elevator contracts as part of your marketing strategy makes farm management sense, especially on that portion of production that can be produced with near certainty, probably the first one-third.

Cash forward contracts, hedged-to-arrive contracts sometimes called futures fixed contracts, and minimum price contracts are elevator contract alternatives that should be looked at for making pre-harvest sales. The best contract for a producer to use largely depends on current and expected futures prices, basis and cash prices.

The put option is an attractive marketing tool because it leaves upside price potential open and does not require delivery. But, that flexibility costs something that must be paid for at the time of purchase. Consider using put options where uncertainty is the greatest, in effect, where uncertainty involves not only price uncertainty but production uncertainty, most likely the second one-third of production sold prior to harvest.

Selling one-third of anticipated production using a cash forward contract or a futures fixed contract and one-third using put options manages an enormous amount of price risk. A floor price is established on two-thirds of anticipated production while the price is still open to the upside on two-thirds.

Crop revenue coverage would enable the producer to sell a greater percentage of the crop on an elevator contract. A producer could contract close to the amount of the production guarantee if the crop is contracted for a price no greater than the base price. Since the production guarantee is valued at the higher of the base price or harvest price, an indemnity payment should generally cover the replacement cost of bushels to fill a contract. There is basis risk, which is a reason to be conservative on the amount contracted.

Crop insurance, elevator contracts and put options are all acceptable farm management methods to manage price risk. All should be a part of the producer's marketing strategy.

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Last updated: July 21, 1999.