

# Farmer's Corner



May/June 2009

Number 3

## Closing the Gap

Everyone has gaps in certain areas of their lives between where they are and where they would like to be. It may not be every area of your life, but no one is perfect and there are areas in everyone's life that could stand for some improvement.

We hear this concept of "closing the gap" in many different forms and in many different contexts. For instance, coaches of sports teams will often say something like, "we just have to continue to go out every day and try to get better" or "we have to continue to build on our success." A common battle cry in the business world is "If you're not growing, you're dying!" These are common sayings that ring true in most aspects of life which is why they have hung around all these years.

This concept of finding ways to improve your situation and closing the gap between where you are and where you hope to be also applies to grain marketing. Simply stated, when it comes to marketing grain each year, everything involved can be divided into two categories: something that helps close the gap or something that keeps you from closing the gap.

### Distractions That Stand in the Way of Closing the Gap

The first thing that comes to mind when discussing grain marketing many times is grain prices. However, this first thought can be one of the biggest distractions that keeps you from attaining your goals. If you look back at history, there is a pretty good explanation of why grain prices became a goal or measuring stick for grain marketing. Prior to 2006, you could look at price histories for the previous 40-50 years and grain prices stayed in a pretty consistent range. The reason is that the technology and overall ability of the farmer to produce grain has consistently risen at a fairly similar rate as inflation. So, a bushel of corn in 1970 vs. 2005 would have cost way more in 2005 if we simply took inflation into account, but since we produce such a greater amount of corn than we did in 1970, it has kept the prices in the same range. Everyone had a good idea in their head as to what price they needed to sell to make good money, average money, or not much money because it had been proven to be pretty similar year in and year out. Then, 2007 and 2008

came along. Prices doubled, tripled, and then quadrupled. Next, prices began to fall rather steeply. It was just enough to make anyone's head spin. With everything in flux, it was and still is hard to figure out which price would make you good money, average money, or not much money. However, all the volatility has taught a great lesson: the price per bushel is not the significant piece, how much money gets put on the bottom line is what matters.

Input costs are another area that can get you distracted from closing the gap between where you are and where you want to be. Of course input prices are important and critical to managing in any business, not just farming. However, they can sometimes cause an unnecessary panic or exaggeration. This has certainly been the case with fuel and fertilizer over the last couple of years. For instance, fuel prices are down around \$2 per gallon now. The worry that we could go back to \$4 fuel as quickly as we fell from it has been something

that has kept farmers from locking in prices this year. Many would say they would probably need another 30-50 cents/bu. on corn if that were to happen. However, upon working through the numbers, in many areas of the country, a jump in fuel from \$2 to \$4 would only change their breakeven costs by 5 cents/bu. Of course, it is different depending on your situation, but it is something worth figuring out for yourself rather than sensationalizing the consequences of an increase in any of your input costs.

One significant distraction in grain marketing is worrying about what basis the grain is sold for. Ultimately, the point of grain marketing is securing as much profit as possible. One thing that has stayed consistent even through the recent volatility in the grain business is how basis reacts. Basis is not a very complicated idea. When a lot of grain is being sold, basis lowers. When not much grain is being sold, basis rises. Basis acts as a tether to keep prices where they need to be to keep grain moving. When basis is strong, it is typically because prices are low and no one is selling. When basis is weak, it is because prices are high and everyone wants to sell. So, those who want to sell the highest basis end up selling at the lowest prices. Basis really has no effect on your bottom line. Selling at good, profitable levels does affect your bottom line. Over the years, the most successful grain marketers have consistently sold a lower basis, but yet a higher price.

Another large distraction in grain marketing can be confusing marketing plans or contracts. These sorts of complicated ways to market grain reinvent themselves with new names year after year. The recurring theme with all of them is that they are something hard to understand and usually involve a lot of futures or options transactions to be put into place. A lot of the time you don't even know how they are doing it on their side, just what they are offering you. The best plan or contract is something very straightforward and simple that allows you to know exactly what price you are getting and exactly how many bushels you have sold and will not change any of those terms after you have signed the contract.

### **Ways to Close the Gap**

When you talk about the concept of “closing the gap” in your grain marketing, the gap simply means the difference from how much profit you are making and how much profit you could be making. It's important to note here that trying to hit a marketing homerun and sell the highest possible price

is not only statistically impossible, but very dangerous to the future of your farming business. So what should you focus on to close your grain marketing “gap”?

First and foremost, there must be a focus put on profit per acre. The dangers of focusing on price per bushel have already been examined previously. That consistent price range lulled everyone into knowing about where a good price was. However, the reason you knew it was a good price was because it made you good profit year in and year out. The goal of any business (farming included) is to make more money than you spend consistently over a long period of time. Everything else is no more than a tool that can help you accomplish this goal. When too much focus is put on one tool to the point that you lose focus on the main goal (profit), bad things can happen. Staying focused on what profit you want to make and then figuring out the other pieces in terms of how they can help you accomplish your profit goal is the key to success in business. So, set a profit per acre goal for the farm and then figure out what price you need to make that happen. The next step is action. Take the price when it gets there! Ignore the noise that tells you it could go higher or the greed that tells you to hold out for more.

One of the simplest ways to improve your grain marketing is discipline. Create a profit-based, disciplined plan of how to market your grain that you can use every year no matter what. The key then is the discipline to stay with the plan every year and never stray from it. Sure there will be years where you could have gotten more, but that's true every year. The old adage applies here – You can't go broke making a profit!

Lastly, close your gap by focusing on your area of expertise. It is easy to spend a lot of your time trying to figure out which way the market will move throughout the year, but the truth is you don't need all the overhead of a farming operation to make money on changes in grain prices. All you'd need is a futures account. Rather than spend your time figuring out if you should take \$3.80 on corn or wait for \$4.00, spend your time doing what you do best – growing a better crop. If you remember that the focus is profit, your time may be better served figuring out a way to squeeze a few more bushels per acre out of your crop than getting a few more cents in the price. There is more money in \$3.80 corn if you grow 170 bushels per acre than there is in \$4.00 corn if you only grow 160 bushels per acre.

**Close Your Gap! Focus on Profits! Be Disciplined! Take Action!**