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.

NOTE: Port Adelaide lentil values have varied between AU$125/t and AU$800/t over the past 7 years (representing variability of 30–100%). For a property producing 200 t of lentils this means $25,000–$160,000 difference in income depending on timing of sales.

Figure 1: Intra-season variance of Port Adelaide Lentil Values.
Source: Profarmer Australia

15.1 Selling principles

The aim of a selling program is to achieve a profitable average price (the target price) across the entire business. This requires managing several unknowns to establish the target price and then work towards achieving that target price.

Unknowns include the amount of grain available to sell (production variability), the final cost of that production, and the future prices that may result. Australian farm-gate prices are subject to volatility caused by a range of global factors that are beyond our control and difficult to predict.

The skills growers have developed to manage production unknowns can be used to manage pricing unknowns. This guide will help growers manage and overcome price uncertainty.

15.1.1 Be prepared

Being prepared and having a selling plan are essential for managing uncertainty. The steps involved are forming a selling strategy and a plan for effective execution of sales.
A selling strategy consists of when and how to sell.

1. **When to sell**
   This requires an understanding of the farm’s internal business factors including:
   - production risk
   - a target price based on cost of production and a desired profit margin
   - business cash-flow requirements.

2. **How to sell?**
   This is more dependent on external market factors including:
   - time of year determines the pricing method
   - market access determines where to sell
   - relative value determines what to sell.

Figure 2 lists the following diagram lists key selling principles when considering sales during the growing season.

**Figure 2: Grower commodity selling principles timeline**

Source: Profarmer Australia

**NOTE:** The illustration demonstrates the key selling principles throughout the production cycle of a crop.
15.1.2 Establish the business risk profile (when to sell)

Establishing your business risk profile allows the development of target price ranges for each commodity and provides confidence to sell when the opportunity arises. Typical business circumstances and how to quantify those risks during the production cycle are described below.

**Production risk profile of the farm**

Production risk is the level of certainty around producing a crop and is influenced by location (climate and soil type), crop type, crop management, and time of the year.

**Principle:** “You can’t sell what you don’t have” – don’t increase business risk by overcommitting production.

Establish a production risk profile by:

1. Collating historical average yields for each crop type and a below average and above average range.
2. Assessing the likelihood of achieving average yield based on recent seasonal conditions and seasonal outlook.
3. Revising production outlooks as the season progresses.
Figure 4: Typical production risk profile of a farm operation.

Source: Profarmer Australia

**NOTE:** The quantity of crop grown is a large unknown early in the year, but not a complete unknown. “You can’t sell what you don’t have” but it is important to compare historical yields to get a true indication of production risk. This risk reduces as the season progresses and yield becomes more certain. Businesses will face varying production risk level at any given point in time due to rainfall, yield potential, soil type, commodity etc.

**Farm costs in their entirety, variable and fixed costs (establishing a target price)**

A profitable commodity target price is the cost of production per tonne plus a desired profit margin. It is essential to know the cost of production per tonne for the farm business.

**Principle:** “Don’t lock in a loss” – if committing production ahead of harvest, ensure the price is profitable.

Steps to calculate an estimated profitable price based on total cost of production and a range of yield scenarios is provided in GRDC’s *Farming the Business Manual* also provides a cost of production template and tips on grain selling v. grain marketing ([http://www.grdc.com.au/FarmingTheBusiness](http://www.grdc.com.au/FarmingTheBusiness)).

**Income requirements**

Understanding farm business cash-flow requirements and peak cash debt enables grain sales to be timed so that cash is available when required. This prevents having to sell grain below the target price to satisfy a need for cash.

**Principle:** “Don’t be a forced seller” – Be ahead of cash requirements to avoid selling in unfavourable markets.

A typical cash-flow to grow a crop is illustrated in Section 11, Figure 5. Lentil during pod-fill and before dry-down on page 6. Costs are incurred upfront and during the growing season with peak working capital debt incurred at or before harvest. This will vary depending on circumstance and enterprise mix. The second figure demonstrates how managing sales can change the farm’s cash balance.
NOTE: The chart illustrates the operating cash-flow of a typical farm assuming a heavy reliance on cash sales at harvest v. a farm business which spreads sales out throughout the year.

When harvest sales are more heavily relied upon, costs are incurred during the season to grow the crop, resulting in peak operating debt levels at or near harvest. Hence, at harvest there is often a cash injection required for the business. An effective marketing plan will ensure a grower is ‘not a forced seller’ in order to generate cash-flow.

By spreading sales throughout the year a grower may not be as reliant on executing sales at harvest time in order to generate required cash-flow for the business. This provides a greater ability to capture pricing opportunities in contrast to executing sales in order to fulfil cash requirements.

When to sell revised

The ‘when to sell’ steps above result in an estimated production tonnage and the risk associated with that tonnage, a target price range for each commodity, and the time of year when cash is most needed.

15.1.3 Ensuring access to markets

Once the selling strategy of when and how to sell is sorted, planning moves to storage and delivery of commodities to ensure timely access to markets and execution of sales. At some point growers need to deliver the commodity to market. Hence, planning on where to store the commodity is important in ensuring access to the market that is likely to yield the highest return.
NOTE: Once a grower has made the decision to sell, the question becomes how they achieve this. The decision on how to sell is dependent upon:

- Time of year determines the pricing method.
- Market access determines where to sell.
- Relative value determines what to sell.

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.

Principle: “Harvest is the first priority” – getting the crop in the bin is most critical to business success during harvest, hence selling should be planned to allow focus on harvest.

Bulk export commodities requiring significant quality management are best suited to the bulk-handling system. 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 7: Grain storage decision making.
Source: Profarmer Australia

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

**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 consist of:
- monthly storage fee charged by a commercial provider OR capital cost allocation where on-farm storage is utilised; and
- the interest associated with having wealth tied up in grain rather than cash or against debt.

The price of carried grain therefore needs to be 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

**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.
Figure 8: Cash values v. cash adjusted for the cost of carry.
Source: Profarmer Australia

NOTE: If selling a cash contract with deferred delivery, a carry charge can be negotiated into the contract. For example in the case of a March sale for March–June delivery on the buyers call at $600/t + $5/t carry per month, if delivered in June this contract would generate revenue of $615/t delivered.

Ensuring market access revised

Optimising farmgate returns involves planning the appropriate storage strategy for each commodity to improve market access and cover carry costs in pricing decisions.

15.1.4 Executing tonnes into cash

This section provides guidelines for converting the selling and storage strategy into cash by effective execution of sales.

Set up the tool box

Selling opportunities can be captured when they arise by assembling the necessary tools in advance. The toolbox includes:

1. Timely information

This is critical for awareness of selling opportunities and includes:
- market information provided by independent parties
- effective price discovery including indicative bids, firm bids, and trade prices
- other market information pertinent to the particular commodity.

2. Professional services

Grain selling professional service offerings and cost structures vary considerably. An effective grain-selling professional will put their clients’ best interest first by not having conflicts of interest and investing time in the relationship. Return on investment for the farm business through improved farm-gate prices is obtained by accessing timely information, greater market knowledge and greater market access from the professional service.
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.
Figure 9: Typical cash contracting as per Grain Trade Australia standards.

The price point within a cash contract will depend on where the transfer of grain title will occur along the supply chain. Figure 10 depicts the terminology used to describe pricing points along the grain supply chain and the associated costs to come out of each price before growers receive their net farm-gate return.
### Costs and pricing points throughout the supply chain

*Source: Profarmer Australia*

Cash sales generally occur through three methods:

**Negotiation via personal contact**

Traditionally prices are posted as a ‘public indicative bid’. The bid is then accepted or negotiated by a grower with the merchant or via an intermediary. This method is the most common and available for all commodities.

**Accepting a ‘public firm bid’**

Cash prices in the form of public firm bids are posted during harvest and for warehoused grain by merchants on a site basis. Growers can sell their parcel of grain immediately by accepting the price on offer via an online facility and then transfer the grain online to the buyer. The availability of this depends on location and commodity.
Placing a firm offer

Growers can place a firm offer price on a parcel of grain by approaching buyers with a set tonnage and quality at a predetermined price. The buyers do not have to accept the offer and may simply say no or disregard the offer.

There are increasingly more channels via which to place a firm offer.

One way this can be achieved anonymously is using the Clear Grain Exchange (www.cleargrain.com.au), which is an independent online exchange. If the firm offer and firm bid matches, the parcel transacts via a secure settlement facility where title of grain does not transfer from the grower until funds are received from the buyer. The availability of this depends on location and commodity.

Anonymous firm offers can also be placed to buyers by an intermediary acting on behalf of the grower. If the grain sells, the buyer and seller are disclosed to each counterparty.

Some bulk handler platforms are also providing facilities for sellers to place firm offers to the market. Including GrainCorp via their CropConnect product.

Finally a grower can place a firm offer directly with an individual buyer.

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. Conducting 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. Considering credit insurance or letter of credit from the buyer.
5. Never delivering a second load of grain if payment has not been received for the first.
6. Not parting 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, alternatively the Clear Grain Exchange provides secure settlement where-by the grower maintains title of grain until payment is received by the buyer, and then title and payment is settled simultaneously.

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.
Relative values

Grain sales revenue is optimised when selling decisions are made in the context of the whole farming business. The aim is to sell each commodity when it is priced well and hold commodities that are not well priced at any given time. That is, give preference to the commodities of the highest relative value. This achieves price protection for the overall farm business revenue and enables more flexibility to a grower’s selling program whilst achieving the business goals of reducing overall risk.

**Principle: “Sell valued commodities; not undervalued commodities”** – if one commodity is priced strongly relative to another, focus sales there. Don’t sell the cheaper commodity for a discount.

Contract allocation

Contract allocation means choosing which contracts to allocate your grain against come delivery time. Different contracts will have different characteristics (price, premiums-discounts, oil bonuses etc) and optimising your allocation reflects immediately on your bottom line.

Consideration needs to be made based on the quality or grades you have available to deliver, the contracts you already have in place and how revenues will be calculated on each contract. Key considerations include; does the contract calculate revenues based on a sliding scale or on predetermined quality ‘buckets’. Whenever you have more grain to allocate than pre-committed to contracts, don’t forget to consider the premiums and discounts available in the current cash market as part of your contract allocation decision.

**Principle: “Don’t leave money on the table”** – contract allocation decisions don’t take long, and can be worth thousands of dollars to your bottom line.

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.

Appetite in pulse markets can be fickle, erratic and the buy-side can be illiquid. Hence monitoring market signals is critical to achieving the best possible returns.

**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:

- 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. In pulse markets the spread between the highest and the second highest bidder can be more than $100/t at times.
- 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.

Sales execution revised

The selling strategy is converted to maximum business revenue by:

1. **Ensuring timely access to information, advice and trading facilities.**
2. **Using different cash market mechanisms when appropriate.**
3. **Minimising counterparty risk by effective due diligence.**
4. **Understanding relative value and selling commodities when they are priced well.**
5. **Thoughtful contract allocation.**
6. **Reading market signals to extract value from the market or prevent selling at a discount.**
15.2 Southern lentils – market dynamics and execution

15.2.1 Price determinants for southern lentils

Australia is a relatively small player in terms of world pulse production, producing 1.5–2.5 million tonnes of pulses in any given year, compared with global production of approximately 60 million tonnes. Lentil is one of the three largest produced pulses across the globe, with 5 million tonnes produced annually. Australia continues to become a growing participant in this market with 200,000–450,000 tonnes produced in recent seasons, accounting for 5–10% of the global crop. Australia, along with the US and Canada are the main exporters of lentil on the global market.

There are two key types of lentil grown across the globe – red and green. Australia primarily grows red lentil varieties which are suited to the lower rainfall climate evident across Australian growing regions. Green lentil varieties continue to be produced in Australia, however volumes remain small due largely to the limited marketing options available. South Australia and Victoria account for 95% of Australian lentil production, which is primarily exported through the container and ‘delivered’ markets. NSW and Western Australian lentil production has grown in recent seasons in response to strong pricing, however volumes remain small. Key production regions for lentils within Victoria are both the Mallee and the Wimmera, while in South Australia production is focused on the through the Yorke Peninsula, Lower Eyre Peninsula, Mid North, and South East South Australia.

The Indian subcontinent is the key importer of pulses globally with the major export markets for Australian lentils including Sri Lanka, Bangladesh, India and Pakistan. Each export market has its own specification requirements and varietal preferences. Hence, it is important to understand the end market of each lentil variety being grown.

The Australian domestic market absorbs only a small proportion of Australian lentil production, with the majority exported primarily to the Indian subcontinent. Given this dynamic Australian farm-gate prices are heavily influenced by global production volatility and international trade values into each of the major destinations.

For example, when Canada, another key global producer suffers below average yields, Australian lentil values tend to find support as global availability of supply is reduced. However, in years when Canadian production is high there is increased competition to secure export business and Australian product can become discounted in order to compete.

Similarly, production issues impacting pulses grown in the Indian subcontinent result in an increase in demand for imported product, providing flow on support to the Australian market. However, in years when production within countries of the Indian subcontinent is in surplus, import requirements are considerably lower, with some becoming net exporters. This reduction in global appetite from key importers due to an oversupply can result in Australian lentil becoming discounted.
Some of the global influences on Australian lentil pricing are listed below:

- The domestic lentil production of both the US and Canada. Any negative influences on production will reduce the global supply and increase the demand for Australian exports.
- Production of lentils within the Indian sub continent. This region is the largest importer of lentils globally, a negative influence on their domestic production places a greater requirement for imports.

### World lentil production calendar

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Figure 11: Global lentil production calendar.

Some of the local influences on Australian lentil pricing are listed below:

- Australian domestic production of lentil.
- Seasonal conditions and the subsequent ramifications on the quality of the Australian lentil crop. With lentil required to meet strict specifications to be exported, adverse weather that impacts the quality over a broad area of the Australian crop has the potential to provide support.

### More information

See Global Pulse Overview – who’s who in the zoo?

Figure 12: Five year average monthly export pace (000t).

NOTE: Australian lentil export pace is typically strongest shortly after our harvest as buyers seek to move crop ahead of the Indian sub-continent harvest.
15.2.2 Ensuring market access for southern lentils

The primary market for the southern lentil crop is exports for human consumption. Production in the southern growing region is focused in north-west Victoria and throughout South Australia, where it is primarily executed through the container or ‘delivered’ market. The southern region is the largest production region in Australia. However given the high value nature of lentils, as well as the counterparty risk of trading into key export regions, the crop continues to be exported primarily in containers.

To ensure access to this market, grain is required to be stored on-farm or delivered directly to the ‘packer’ at the time of harvest. Premiums may be available for lentil stored on-farm, allowing the buyer greater flexibility. However the cost of storage must always be considered.

There is virtually no “fall-back” safety net of a feed price if quality does not meet export food market criteria (and if there is a feed price, it is a much less than for other pulses). Lentils with green kernels are difficult to sell even as feed (bitter taste).

NOTE: Storage decisions should be determined by assessing market access. The large majority of Australian lentil is exported in containers. Hence, private commercial storage and on farm storage can both provide efficiencies to market.
15.2.3 Executing tonnes into cash for southern lentils

Given the volatile nature of lentil pricing, setting a target price using the principles outlined in section 15.2.2 minimises the risk of taking a non-profitable price or holding out for an unrealistically high price that may not occur. Pricing deciles for lentil are provided as a guide.

![Figure 14: Port Adelaide Lentil Deciles. Source: Profarmer Australia](image)

Selling options for lentil include:

1. Store on-farm then sell–Most common occurrence. Lentil is relatively safe to store and requires less maintenance than cereal grains. It does however remain important to monitor and maintain quality, with lentil required to meet strict quality specifications for export in order to avoid being discounted at the time of delivery. Must consider cost of storage in target pricing.

2. Cash sale at harvest–least preferred option as buyer demand does not always coincide with harvest. Values can come under pressure at harvest time if an influx of grower selling occurs in a small window, subsequently providing buyers with confidence they can meet their short or medium term commitments.

3. Warehouse then sell–this provides flexibility for sales if on-farm storage is not available. Must consider warehousing costs in cost of production and target prices. In South Australia this is an alternative option offered through the major bulk handlers. Availability of this option from ‘packers’ within the ‘delivered’ market in both South Australia and Victoria will vary depending on each individual buyer.

There are some forward price mechanisms available for lentil including area contracts, as well as a traditional fixed volume forward contracts. Whilst area based contracts tend to price at a discount to fixed volume contracts, this discount needs to be weighed up against the level of production risk inherent in each contract.

As with all sales, counterparty risk and understanding contract of sale is essential. Counterparty risk considerations is especially important for pulse marketing as there is often a higher risk of contract default in international pulse markets than for canola or cereals due to the markets they are traded into and lack of appropriate price risk tools (such as futures). This can place extra risk on Australian-based traders endeavouring to find homes for your product.
Figure 15: Long-term Port Adelaide lentil price history.
Source: Profarmer Australia