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THE FARMER'S EDGE

Hurley & Associates
Agri-Marketing Centers

Crop Mix Decision Getting More Complicated Across South Plains

By John Miller

While the South Plains does seem to experience a wider range of weather extremes in the growing season than most other U.S. production areas, I do think there are some common trains of thought nationwide when it comes to evolving approaches to determining an upcoming crop mix. Prior to just a few years ago, discussions about rotational needs and market outlook went a long way to deciding what to plant and how to manage inventory. Nowadays however, the planting discussion almost always includes the pursuit of high-end yield potential, avoidance of certain crops based on disease and/or quality loss potential, striving for better grading/discount outcomes, and ease of harvest and transportation. For example, it wasn't that long ago that most dryland cotton farmers across the South Plains found that harvesting a bale per acre to be a nice crop, with irrigators hoping to double that yield. Across these same areas it is now common to at least include inputs and effort for 2 to 3 bale dryland, and 4 to 5 bale irrigated cotton. Dryland corn in these same areas that struggled to make 100 bushels per acre routinely average 150 or more. And we have seen some similar stories with wheat and soybeans at times. It might be a good argument that evolving cultural practices, the adoption of advances in plant genetics, chemical application, farming and handling equipment and ginning technology for cotton over the past few decades are paying off. Favorable weather will always play the biggest part in making the crop a farmer wants, but the last few years makes one wonder if under wider weather conditions that the coming together of modern practices and technology has brought us to expect better yields than just a few years ago. While it takes several years of information to control for a wide range of season-long growing conditions, a pattern does seem to be developing in an area that has long lagged well behind national average yields.

What started to peak my interest in changing perceptions of the crop mix was the fact that I starting seeing decisions on what to plant that did not seem intuitive at first, but later made perfect sense when more of the story was revealed. For example, soybean futures relative to corn seemed to push the farmer more in that direction when using typical planning yields and basis forecast. After going over South Plains customer dryland budgets, the $425 per acre full economic cost of growing soybeans seemed to fair well against an approximately $600 dollar cost for corn using planning yields and prices. The past three years, however, have seen late season weather that has seriously impacted

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soybean plant development, made Green Stem disease harder to control and led to severe quality discounts when sold. A more educated foreign buyer, and more sophisticated testing equipment have made our only market, Gulf ports, more difficult to depend on at harvest given rejection risks. In addition, it is much more difficult to store soybeans on the farm in our climate which makes one more nervous knowing that harvest delivery may be subject to rejected loads and no plan B. For these reasons, we have seen corn acres remain steady despite market signals to do otherwise as corn yields have in recent years become much more stable in a wider range of growing season weather experiences. There is also the perception that the most common corn quality issues are easier to manage once the crop is in storage since there is a much more diversity among users with respect to their ability to use corn of this type. Even sorghums $360 per acre cost estimate breaks down when one considers the wide yield and quality variations that we have experienced over the past few years. The arrival of the Sugarcane Aphid and associated cost of control added to the risks of lodging and/or sprout during the tropical weather season has prompted major change despite a budget that at first glance appears more profitable. Even the prospect of a large PLC payment on cotton generic base seems to have minimal impact on the planting decision.

For our production area, however, there is not a better example of the issues just discussed than with cotton. Even farmers themselves have been dismayed at what their cotton

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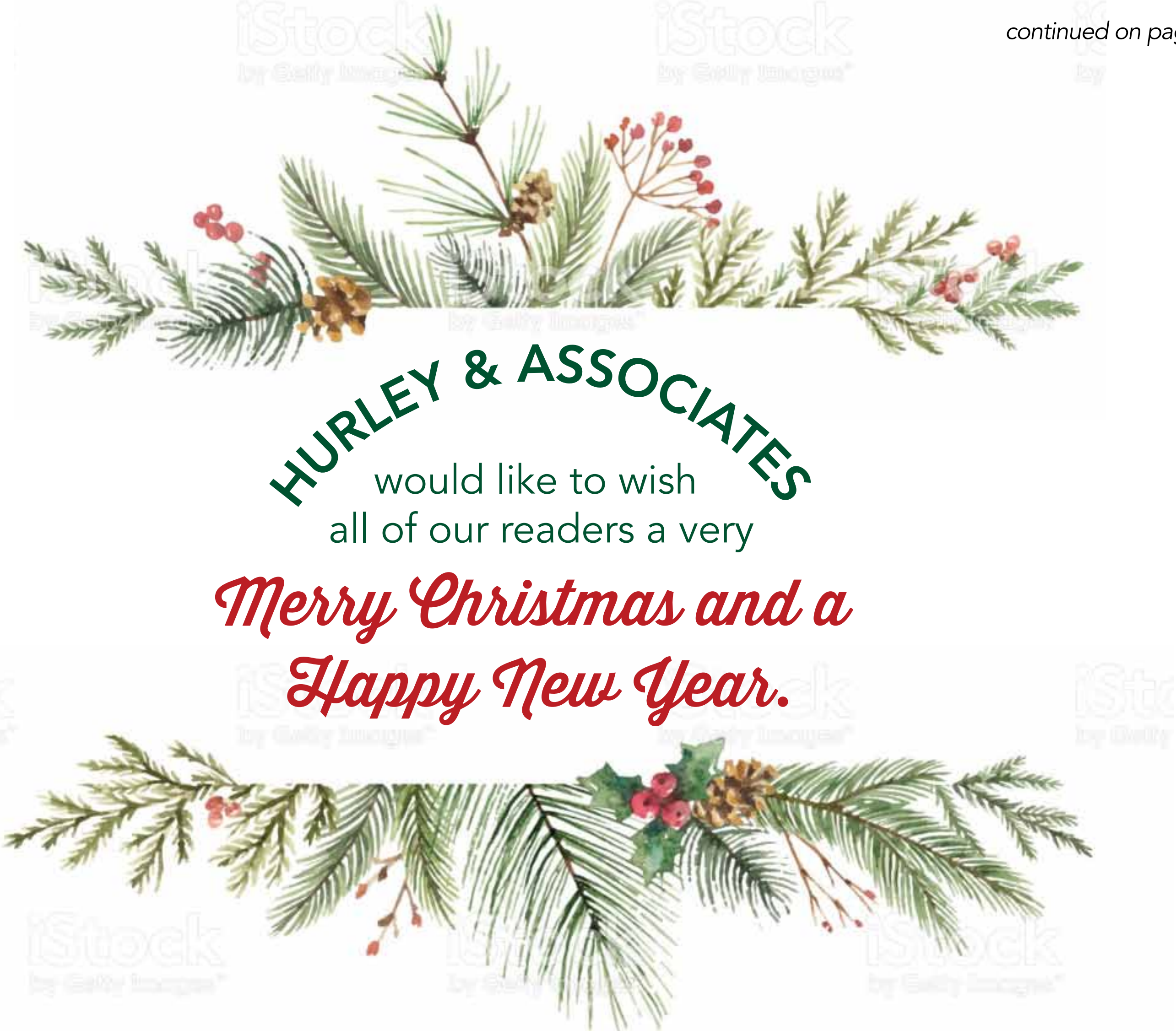

Marketing into the Future

By Ed Case

I've been approached by colleagues asking how I think marketing in the future will be, specifically will it get easier?

The short answer is "probably not", but that doesn't mean you can't make it easier! Successful marketing is all about how you approach it. You can make it as simple or as difficult as you wish. To coin a phrase from the founder of Hurley and Associates, Mrs. Ida Hurley, "simple is hard" which she has stated many times in the past. Simple marketing comes from using the tried and proven method of marketing for profit. Reasonable and acceptable profit not "all I can get profit". Industry standard suggests that 10% to 20% return on investment is a reasonable profit expectation. However, if you incorporate 50% plus return on investment into a marketing plan, you may be dooming yourself to failure by having price targets above what the market can reasonably achieve without some type of catastrophic event to drive prices higher. Be careful what you wish for! It's not in your best interest to wish for a catastrophe to achieve a lofty market plan plus the hardest decisions to make are those that need to be made in the middle of a catastrophe. On the other hand, if a market happening is creating an opportunity to lock in 50% plus return on investment, you need to know that and be proactive to protect that much market equity. Many will argue that this is a lot easier said than done because knowing what is absolutely profitable may not happen until after the crop is harvested to determine exact yields and costs of production and by then the opportunity to sell at a reasonable and acceptable profit may have already passed. I totally agree, but unless you put forth the effort to project your breakeven by forecasting yields and cost of production, you will be left not knowing what you need out of the market to be profitable and risk missing sound marketing opportunities. It's important that you update your breakeven projections throughout the year and finalize them after harvest to stay abreast of your changing operational needs. Even though projections are subject to change until finalized, updated projections are the most reliable source we have to help measure the value of the market at any point in time. How we choose to protect market value at the time can vary from one operation to the next.

This is why OPTIONS were created, to give you the confidence to make the hard decision and the right decision in the face of uncertainty, especially uncertainty that exists as a result of a catastrophic event. Uncertainty drives the market and creates opportunity! How many times have you missed a great marketing opportunity because uncertainty kept you from pulling the trigger? Have you ever heard the excuse; "I didn't think I could sell what I wasn't sure I was going to have so I did nothing", besides everything I read and heard about the market at the time said the market was going higher and I didn't want to miss out on higher prices. Lack of execution is the main reason for marketing failure! That will never change so we have to be more disciplined in our approach. Opportunities can be VERY short lived so one needs to be prepared to act quickly. Learn how to use and incorporate minimum risk strategies that allow you to execute with confidence when you are struggling with pulling the trigger. Investing in an Option strategy when a high degree of individual uncertainty exists allows one to proactively protect market equity at a time of opportunity and avoid any delivery commitment associated with a cash contract. It also leaves additional upside opportunity open with your unsold cash bushels. A simple PUT OPTION protects against downside price risk without a delivery commitment and allows your unsold physical production to take on additional value if the market continues moving higher. You also retain beneficial interest in your physical production to shop to the cash market of your choice when you choose to cash convert. That should allow you to rest more peaceful at night knowing that your marketing is well positioned whether the market goes higher or lower!

The acceptable and practical principles of marketing that are successful today are the same principles that will make for successful marketing into the future;

1. Determine your breakeven (total cost of production divided by estimated yield per acre of each crop enterprise). Ex; Corn - $700.00 / acre cost divided by 200 BPA = $3.50 per bushel breakeven.
2. Keep estimates updated throughout the growing

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crops have done in the face of what in years past would have been considered difficult growing years. The once radical cotton yields that have become common across the South Plains in recent years has definitely helped the national average cotton yield to trend upward; and the increase seen over the past 3 years has coincided a move from 8.5 to 12 million acres, suggesting that it is not the loss of marginal ground that is helping to boost yield as is many times the case. Cotton is also a case where quality has been improving under a wider range of weather experiences which can be an important boost to the bottom line due to the way cotton premiums are established and paid. While quality aspects are still very weather sensitive, it does seem that seed technology and practices are making a big impact. Even our findings of an estimated $650 dollar per acre full economic cost on dryland seemed to draw little attention relative to other crops as virtually all South Plains growers hope to achieve 2 to 3 bale dryland yields. There is a myriad of other factors that had made cotton more attractive than just a few years ago. But the underlying fact is that improving yields and quality under broader weather experiences along with advances in harvest, ginning and transportation processes have seen cotton acres grow in the face of formerly unattractive price environments. These factors affecting the planting decision for cotton are virtually identical to those keeping soybean acres in check versus corn despite a yield and price outlook that might suggest otherwise.

Working with a diverse clientele across the greater South Plains, I can attest that farmers there are spending more time searching for greater overall efficiency on the farm so that the operation can remain profitable under a wider range of yield and price outcomes. The volatile price environment that may, or may not, provide profitable opportunities at average yields places a lot of pressure on farmers to maximize potential in the field. Farmers are first to understand that all of this new technology that is pointing to a new plateau in yields comes at a cost. And for the first time we are seeing wide spread efforts by farmers to get landlords to share in their costs. As our discussion about uncertain prices suggests, it will be creative efforts by all stakeholders in the crop including farmers, landowners, scientist and those providing products and services to the industry that keep farming across the Southern Plains as viable and widespread as it is currently.

Consultant Spotlight:
Jared Knudson

What do you most enjoy about your job?
The clients I serve. One of my life goals is to spend as much time as possible with people I enjoy being around. Working with farmers (and more specifically my clients) provides me with an opportunity to do just that.

How did you get started in your career?
I started with John Deere Credit in Johnston, IA out of college. I had a very non-glamorous job in the documentation group that involved delivering mail and faxes to other parts of the department. Like most college grads, I thought I was going to light the world on fire immediately so this was a humbling experience in many ways. But in hindsight, I wouldn't change a thing. Taught me that everything is earned and to appreciate where you've been.

What are you most passionate about when it comes to serving our clients?
Just making a difference in their lives and operations. We are reminded all too often that the Ag economy isn't terrific right now, but it's a challenge that I take head on. I enjoy the opportunity to be a part of leading producers through the current environment.

What would be your ideal vacation?
Tough question – someplace quiet without a lot of distractions. A cabin somewhere in the mountains (like Alaska or Montana) would be great.

Jared grew up in Eastern South Dakota. He has been involved entirely in Agriculture since graduating from South Dakota State University in 2002 with a degree in Business Economics. His professional experience includes time with John Deere Company and two privately-owned John Deere dealerships. Most recently, he oversaw the Parts and Service Departments for Schuneman Equipment Co., a six-store John Deere dealer with locations in Eastern SD and Western MN.

Jared joined the Hurley team in 2013. He has a passion for helping producers, an affinity for the agricultural markets and believes in Hurley's risk management approach to marketing. Jared lives in Brookings with his wife, Katie, and their children.

A Leader's Legacy

By Jackson Waage

What defines a leader's true legacy? Does having a singular linchpin set up an operation for long-term success?

These are two questions posed by Simon Sinek in his book "Leaders Eat Last".

In the chapter titled "Lead the People, Not the Numbers", Sinek discusses the differing leadership styles of Jack Welch, former CEO of General Electric, and James Sinegal, former CEO of Costco, as well as his conclusions drawn from it.

As the U.S. was recovering from a financial downturn in 1970's, a new economic theory titled "Shareholder Value" was created. It stated that the true measure of a company's success was defined by how well its stock price performed. Though the theory sounded good, it created a conflict of interest as company CEO's were now being paid primarily based on stock price performance, therefore incentivizing them to maximize profit, even at the cost of customers and employees.

Jack Welch led General Electric (GE) from 1981 to 2001. During his tenure, Welch was well known for his practice of laying off the bottom 10% of his managers at the end of every year. By executing this plan, he was able to maximize the company's profits on paper, strengthen the company's stock price, and therefore increase his salary. Under the premise of "Shareholder Value", Welch was astonishingly successful and considered one of the most prosperous businessmen of his time.

Though on paper Welch was successful, there were flaws in his approach. With employee's living in constant fear of falling into the bottom 10%, innovation suffered. The financial success of GE in the 80's & 90's had a foundation

based on short-term profit maximization and no eye on the future. Once Welch retired and was succeeded by Jeff Immelt, GE saw its stock price fall from $51.86 at its peak in May 2001 to $22.48 by February of 2003.

James Sinegal, CEO of Costco from 1983 to 2011, had a contrasting leadership style. Costco treated employees as family, and targeted low turnover as a key factor to success. Though Wall Street moguls mocked Sinegal's business practices, he continued to pay more than double minimum wage to hourly employees and offered 90% of its workers employer-sponsored health insurance, even though the industry average is below 60%.

Sinegal's greatest success, however, was credited to his willingness to be open to new ideas created by employees and willingness to distribute power throughout the company. This allowed him to keep a keen eye open on the future plans.

The environment created by his predecessor has allowed current CEO, Craig Jelinek, to continue Costco's financial success. Since Jelinek took over, Costco has seen its stock price rise from $84.66 in December 2011 to today's price of $172.69.

Sinek concludes that we need to judge a leader not on what they do while holding the torch, but in what happens after they pass the torch on. A leader's true legacy is defined by the strength of the foundation left behind, not the individual

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Economic Round-Up

By John A. Johnson

An article on our domestic economy is enjoyable to write this month, as we see housing prices on the rise, inflation low, unemployment virtually non-existent and interest rates in a very stable and benign mode for what appears to be the long haul. The new Fed chief, Jerome Powell, is expected to maintain the same rather low-interest proclivities as his predecessor, Ms. Janet Yellen. When we add in a stock market hovering near all-time record highs and consumer confidence at a 17-year high, what's not to love?

Only the agricultural sector seems to be lagging behind in sharing the bounty of some of the best economic times in the history of our country. More specifically, our row crop producers seem to be suffering from their own productivity. Massive surpluses of almost every row crop commodity stuff warehouses and burden supply lines. This is truly a buyer's market in global commodities, as consuming nations dictate prices to producers for a change. U.S. wheat for example, has been shut almost completely out of world trade as Russian Black Sea wheat dominates sales on a weekly basis. Cotton prices languish at the same levels that were common in the 1980's, only massive increases in production efficiency and yields have made cotton producers able to maintain any level of profitability.

In the livestock sectors, dairy producers are also feeling the sting of over production and are struggling to stay afloat amidst flat prices as input prices for everything except feed rise higher and higher. If and when grain and protein prices start to rise, dairy producers will either have to see prices for their production increase, or see a serious drawdown in the number of cows, farms and operators.

Beef, pork and poultry producers on the other hand, are enjoying good profits while consumer spending is high and protein products are in big demand, both domestically and for export. Brazil continues to struggle with fall out from their packing house scandals, and Australia is in the midst of a re-building phase for their cow herd. Canada and Mexico do what they can to bridge the gap, but world demand for beef is still very good and U.S. imports lag behind year-ago levels, mostly due to limited availability.

U.S. farmland prices have begun to soften in several markets with recent sales running from 3-10% below last year's already-lower values. Ironically, rent for first class, highly productive land has not lagged as much on a percentage basis as overall land values. We would venture that ever-optimistic producers are holding on to some rented acres, even if they aren't wildly profitable, in the hope that the rampant prosperity of the past decade will soon return. They don't want to be in the position of giving up and throwing in the towel to reduce acreage too early.

Globally there is somewhat a different economic story as Europe reels from the effects of British exit from the European Union, and Germany tries to sort out the results of what looked like was going to be a complete upheaval in Ms. Merkel's government, only to arrive back full-circle to about where they started, with the same mix of liberal and conservative members of the Bundestag forming an uneasy coalition. With so much chaos surrounding two of the most important members of the Union, confusion reigns.

China is finally getting serious about their pollution problems. So serious in fact that they have detrimentally affected many of their manufacturers' productivity. Anecdotally, one contact in the farm chemical supply business informs us that Chinese production of farm chemicals is slowed down so much that product is difficult for many companies to source right now. We don't expect that to change much by the time we start the 2018 U.S. crop.

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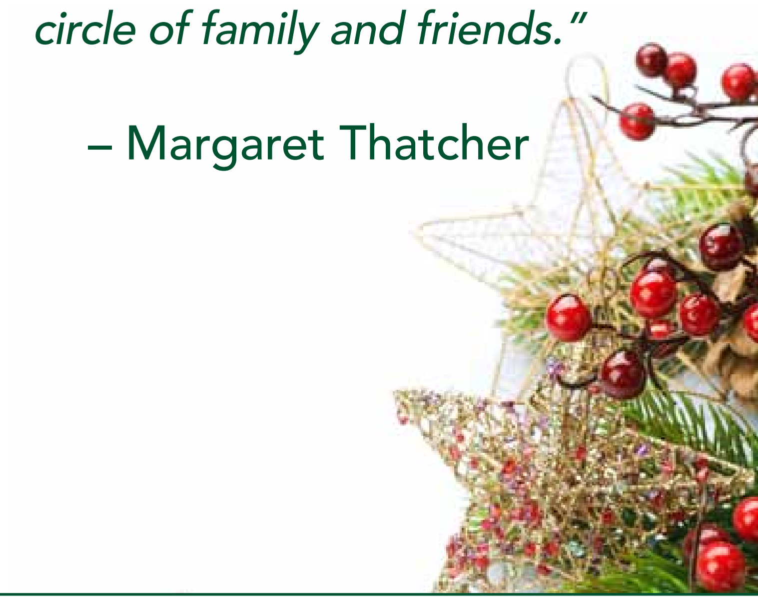
season. Remember they are a projection and subject to change until finalized. How they change could alter your marketing decisions.

3. Prepare a market plan of action that includes targets and strategies which reflect you're goals and effectively manages uncertainty risk. Be prepared to alter your plan to address changing market conditions and/or changing projection estimates.
4. Execute the plan with confidence. The biggest reason for success or failure!

The fact is nobody knows for sure what the market is going to do. Predicting the market with any degree of accuracy has everything to do with predicting future events that will affect the market and to what degree. Holding out for "all we can get" or the top of the market is just not practical and is VERY risky at best. The most we can hope for is a marketing opportunity that allows us to cash convert our production at acceptable and profitable levels. That is why we raise the crop in the first place, besides the love of being a farmer!

"Christmas is a day of meaning and traditions, a special day spent in the warm circle of family and friends."

– Margaret Thatcher



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success created during their tenure.

As Sinek describes passing a business from one CEO to the next, it felt as if he was describing the passing of a family farm from one "CEO" to the next. From a business standpoint, taking a step back and honestly asking oneself:

Have I created an environment in which I am not needed for the family farms future success?

As we wrap up another fall's work and enter into the Holiday season, challenge yourself to sit down with your shareholders (family, partners, employees) in the coming months and discuss a few of the following big picture ideas:

- Why do we farm?
- What are our long-term goals?
- Is the current business plan sustainable for future generations?
- If I were to disappear today, would the farm continue to flourish?
- Am I allowing my employee's (brother, son, daughter, hired man) voices to be heard?
    - o Do I take their ideas seriously?

Though there are a million different ways to define successful environments and sustainable plans, the goal of this article is to try and pull your mind away from day to day tasks, and to start thinking about what your future may hold.

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