Difference between Cow/Calf Operation and Stocker/Grower & Feedlot is….

• Cow/calf enterprise is a fixed cost operation

• Stocker/Grower & Feedlot are margin operators (packer and retailer are also margin operators)

• Margin operators focus on the buy and sell

• Margin operators manage their inputs
Margins by Sector: Cost Structures

• **Cow/calf**: BUYS labor, fertilizer, fuel, equipment

• **Genetics; SELLs calves**

  Bulk of costs are not linked to sales

• **Stocker / Feeder**: BUYS cattle, feed, etc; SELLs cattle

  Costs are linked to sales, profit opportunities in high/low markets
What is “Risk Management”? 
Risk Management

Credit Availability & Worthiness & Rates
Purchase and sale price risk
Basis risk
Corn and protein cost risk
Fuel, energy and fertilizer price risk
Animal Health
Performance predictability
Currency risk
Government Regulation and Policy
Stocker and Feedlot Risk Management

- Develop marketing strategies with a “whole operation” view, enterprise Risk Management and Margin analysis.
- Know the seasonal trends of market. Utilize seasonal marketing as part of Risk Management.
- Don’t deviate from plan.
- Stay plugged in with your CattleFax analyst to monitor trends, basis, and price expectations.
Things to know:

- Breakevens (Corn impact on breakeven)
- Analyze cash fundamentals trend (up, down, sideways)
- Analyze basis trend (strong, weak, sideways)
- Analyze futures technical trends (up, down, sideways)
- Set realistic profit objectives/narrow losses - ROI
- Have flexibility to change

Key: Have the discipline to follow through and act on profit opportunities and trend changes
A Few Key Points

• Per head P/L is NOT ROI – why?
• Profitability varies WIDELY within sectors
• Volatility is extreme and will increase as market goes up.
## Annualized Return on Equity (ROE) vs. Head Profit Given $150 per Head Collateral

<table>
<thead>
<tr>
<th>Days On Feed</th>
<th>Dollars per Head Profit</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$10.00</td>
</tr>
<tr>
<td>100</td>
<td>24%</td>
</tr>
<tr>
<td>120</td>
<td>20%</td>
</tr>
<tr>
<td>140</td>
<td>17%</td>
</tr>
<tr>
<td>160</td>
<td>15%</td>
</tr>
<tr>
<td>180</td>
<td>14%</td>
</tr>
<tr>
<td>200</td>
<td>12%</td>
</tr>
</tbody>
</table>
U.S. Consumer Expenditures on Beef

Source: USDA
Projected 2011
U.S. net beef supply valued at all-fresh retail
How is the Money Allocated?

LEVERAGE

- Cattle/beef industry segments remain largely independent of each other
- Equity, management, financially
- Markets allocate revenue – AND – LEVERAGE drives markets
Ethanol % of Usage vs Cost of Gain
Fed Steer Price Volatility -
(cumulative change from week-to-week)
**PRICE VARIABILITY INCREASES AS THE MARKET RISES**

*Historically the average price range from high to low during the year is 21%*

<table>
<thead>
<tr>
<th>Annual Fed Price</th>
<th>21% Price Range</th>
<th>High to Low Variation</th>
<th>Increase in $/Head</th>
</tr>
</thead>
<tbody>
<tr>
<td>$80</td>
<td>$72.50-87.50</td>
<td>$188</td>
<td>$0</td>
</tr>
<tr>
<td>$90</td>
<td>$81.50-98.50</td>
<td>$213</td>
<td>$25</td>
</tr>
<tr>
<td>$100</td>
<td>$90.50-109.50</td>
<td>$238</td>
<td>$50</td>
</tr>
<tr>
<td>$110</td>
<td>$99.50-120.50</td>
<td>$263</td>
<td>$75</td>
</tr>
</tbody>
</table>

Assumes 1250 pound live weight
Credit Needs Skyrocket

Annual Average Fed Steer Value ($/Head)

It takes 64% more capital/credit to operate in the current environment

1995-2002 Avg
$791 per head

Years

CattleFax | THE DECIDING FACTOR
Summary

• What is your Business?
• Volatility
• Capital
• Plan
Risk Management for Cow/Calf and Stocker Operators
2011 and Beyond

- **Cow/calf Profits:** Tighter supplies, good export demand, improving domestic demand
- **Efficiency Growth:** Fewer animals producing more meat
- **Demand Driven Markets:** Tightening supplies drive prices higher; sharply higher with DEMAND improvement
- **Commodity Volatility:** Outside money will continue playing a bigger role in commodity pricing
- **Will the U.S. Embrace Trade Again?:** Critical to U.S. ag expansion
Marketing Calves

- **Seasonality:** The biology of cattle and forage lead to large seasonal supplies of calves
- **Marketing Mechanisms:** Forward contracts allow producers to price ahead of delivery
  - Pro’s / Cons: direct contract, video sales
  - Why not hedge using feeder futures?
    - Poor basis predictability

**Good marketing strategies require knowing your breakeven cost of production, ie: $95/cwt**
Seasonal 550 lb Steer Price

Source: CattleFax
550 lbs Steer Annual Price Range and Average

MIN  MAX  AVG

Source: CattleFax 2011 Forecast
Seasonal 750 lb Steer Price

Source: CattleFax

1991-2010

INDEX

WEEKS

CattleFax | THE DECIDING FACTOR
**750 lbs Steer Annual Price Range and Average**

- **MIN**
- **MAX**
- **AVG**

Source: CattleFax 2011 Forecast
Seasonal Fed Steer Prices

1991-2010 Index

Source: CattleFax
Seasonal Utility Cow Price

1991-2010

Source: CattleFax
Video Sales

- Sign up and commit a commission premium to list cattle on sale; typically a portion is refunded if you “pass” on the sale price
- Cattle are filmed in advance
- Auction televised and/or on the internet
- Buyer remits down payment on contract for later delivery
- Defaults are very rare
- Opportunities for value-added cattle
Cow/Calf Risk Management

- **Buy**: labor, fuel, fertilizer, diesel, equipment, bulls, hay/forage
- **Sell**: calves, feeder cattle, cull cows

While there are limited opportunities to manage input cost risk, this section will focus on the sell side of risk management.
Difference between Cow/Calf Operation and Stocker/Grower & Feedlot is….

• Cow/calf enterprise is a **fixed** cost operation

• Stocker/Grower & Feedlot are **margin** operators (packer and retailer are also margin operators)

  • Margin operators focus on the buy and sell

  • Margin operators manage their inputs
Cow/Calf Risk Management: Retaining Ownership
Fall Weaned 550# Calf

Dry Lot Winter (Oct-Apr, 175 days)
- 725 lbs
  - Summer Grass (Apr-Sep, 160 days)
    - 1,000 lbs
      - Feedlot (Oct-Dec, 100 days)
        - 1,300 lbs

Precondition (Oct-Nov, 35 days)
- 600 lbs
  - Feedlot (Nov-Jun, 230 days)
    - 1,290 lbs
      - Winter Grazing (Nov-Apr, 130 days)
        - 850 lbs
          - Feedlot (Apr-Aug, 150 days)
            - 1,300 lbs

Background (Oct-Jan, 100 days)
- 800 lbs
  - Feedlot (Jan-Jun, 160 days)
    - 1,300 lbs
Hold for Summer Grazing

- Balance ranch to keep 100% stocked (easier to increase/decrease yearlings than cowherd; 80/20, 60/40 etc)
- Summer grazing gains are very competitive when corn is expensive
- Can I winter calves cheaply? Keep calves from getting too big
- Does it make sense to price my calves early and sell, THEN buy cheaper fall calves for grazing?
Before you make the decision to send your cattle to a feedyard, consider these questions:

- What type of cattle do they normally handle?
- What type of marketing programs do they use?
- What are the ration costs (as fed, dry, moisture content)?
- How are they going to charge yardage?
- Can they run a projected breakeven for you?
- Will they partner on ownership of your cattle?
- Can they help with grain and cattle risk management?
- Is carcass information available?
- Who are some previous customers I can talk to?
Things to know:

✓ Cost of production
✓ Breakevens (be conservative)
✓ Analyze cash fundamentals trend (up, down, sideways)
✓ Analyze basis trend (strong, weak, sideways)
✓ Analyze futures technical trends (up, down, sideways)
✓ Set realistic profit objectives/narrow losses
✓ Have flexibility to change

Key: Have the discipline to follow through and act on profit opportunities and trend changes
Components of Cash Price

CASH PRICE equals FUTURES + BASIS

- **FUTURES**
  - Futures prices will make up the majority of cash price
  - Live cattle and feeder cattle futures are traded at the Chicago Board of Trade (CME Group).
  - There are two types of factors that influence futures: A: Fundamental; B: Technical.
  - Fundamentally, futures are a reflection of domestic and global supply and demand.
  - Placements, growing/feeding conditions, fed cattle currentness, production levels and export demand, are all examples of **fundamental** factors influencing the futures market.
  - Stochastics, support and resistance, trends and moving averages are examples of **technical** factors influencing the futures market.

- **BASIS**
  - **Basis = Cash – Futures**
  - Once hedged, your risk shifts to the basis.
  - Basis risk can be avoided by establishing a basis contract.
1. PROFIT OBJECTIVE****

2. Cash Trend

3. Futures Trend (Technical)

4. Basis Opportunity

*Most important overrides all others*
Utilizing Historical Basis

- Projecting basis for the respective delivery period
- Key to estimating your breakeven
- Premiums/discounts need to be accounted for

<table>
<thead>
<tr>
<th>850# Oregon Steer Basis - January Futures Contract</th>
<th>850# Nebraska Steer Basis - January Futures Contract</th>
</tr>
</thead>
<tbody>
<tr>
<td>December</td>
<td>-6.59</td>
</tr>
<tr>
<td>January</td>
<td>-6.87</td>
</tr>
</tbody>
</table>

Example: January 2011 futures trading at $119/cwt, historical basis equal -$7.00, Then your projected cash price equals $119+(-$7) = $112/cwt
Cow/Calf and Stocker Risk Management

- Develop marketing strategies with a “whole operation” view
- Analyze costs on a breakeven ($/cwt) basis; run the numbers
- Know the long-term, annual, and short-term seasonal trends; utilize seasonal marketing
- Stay plugged in with your CattleFax analyst to monitor trends, basis, and price expectations
Strategy: Maximization of Resources

February 2011
What Is Your Ultimate Strategy/Goal?

Long-term sustainability:
• Profitability / Asset appreciation
• Growth
• Resource preservation
• Succession planning

Short-term Capital Gain:
• Asset appreciation
• Buy/sell strategy
Peak Efficiency and Profitability Requires Maximization of Resources:

- Forage
- Equipment
- Land Base
- Equity: Access to Capital
- Knowledge / Skills
- Business Relationships
Maximization Strategies: Forage

• Consider all options for utilizing forage:
  • Cows
  • Stockers
  • Wildlife
  • Harvest
  • Recreation
  • Leasing strategies (swap for more advantageous forage)
Maximization Strategies: Equipment

- New paint is expensive! Consider all options
  - Leasing (seasonal needs)
  - Sharing (I buy a swather, you buy a baler)
    - Be careful here: communicate usage, repairs, hour allocation, etc!
- Is custom harvesting an option?
  - Hire out your services and equipment
  - Hire someone for your harvest needs

Bottom Line: Consider all equipment costs in your calcs (depreciation, interest, repairs, maintenance)

Example: annual baler cost ÷ bales harvested = $__/bale
Maximization Strategies: Land Base

- Land is more than just land!
  - Mineral rights?
  - Wind resources?
  - Water resources?
  - Hunting?
  - Recreation?
  - Swap land through leases or deeds?
Maximization Strategies: Equity / Access to Capital

• What does your balance sheet show? Net worth

• What is your borrowing capacity and interest rate?

• Think of your equity as a separate profit-center; how do you put your equity to work, earning a greater rate of return than your interest rate?

• Ag or non-ag based; leverage land to buy and apartment complex in town that cash flows and pays for itself?
Maximization Strategies: Knowledge/Skills

• What are you good at? Passionate about? What do you do better than most?
• Can you get certified/licensed for a skill?
• What are your time constraints? Seasonality?
• What about other family members on the operation?
Maximization Strategies: Business Relationships

• Are there additional resources in your “network”?

• Expanding your network beyond the cattle world

*Examples:*

• Does your doctor need a place to hunt?
• Do you have a relative or friend who would like to invest in land (and lease it to you)?
• Can you custom precondition calves for a feedyard?
Summary

• Sustainability = Long Term Profitability
• The cattle business is no longer just about cattle
• Higher costs of land, cattle, and equipment necessitates “thinking outside the box”
• Get comfortable running numbers, spreadsheets, and projected financials

Are your resources maximized?
Thank You

www.cattlefax.com

800-825-7525