

# Managing Risk with Specialty Grains

*Number 4 in a series of marketing columns from Purdue University specialists.*

by Kathleen Erickson, Joan Fulton and Frank Dooley

Balance. It's imperative to successful management, leadership and just regular old life! But when it comes to managing risk from specialty grains, grain handlers find themselves in a unique position — a balancing act dealing with several sources of risk.

Risk is uncertainty about an outcome. It is no news to any of us that while specialty grains have generated some business opportunities, they have also generated some new business risks and a whole new set of challenges. In this column we will explore the different sources of risk and provide some insight on managing these new challenges.

For the purpose of this month's column, let's focus on risk using grain handlers as the example. Grain handlers daily face risks in financial, legal and marketing issues. Firms wishing to reduce their marketing risk need to focus on these areas: *Marketplace Awareness, Relationships with Grain Producers, Relationships with Grain processors or Customers.*

Of course, while these efforts will help manage risk, they won't completely eliminate it. When operating within a more responsive supply chain, operational flexibility is a must.

## Risk's Key Issues

Regardless of the size of your company, how you manage risk (how you balance) can set you apart. For firms handling specialty grains, risk is related to: *Market price, Quantity, Quality and Shipping timing issues.*

First of all, let's consider marketplace changes and the price risk that results. Price risk associated with fluctuating market prices is a major source of risk, just as with #2 yellow corn. Just because you are handling specialty grains you are not immune from market fluctuations. After all, the specialty grains are often priced as a premium over the commodity price. Just as hedging on the

Chicago Board of Trade (or other commodity exchange) is an effective way to reduce price risk when handling commodity grain it is also a useful tool when handling specialty grains.

However, the unique traits associated with specialty grains result in additional risks. Quality and quantity are other sources of risk. Quality concerns are twofold: being able to deliver grain tested for specific types of requirements, such as genetic origin, and having grain with enough levels of the desired characteristics, such as oil content. For example, an elevator may have high oil corn, but not the particular hybrid the customer requires; or the



elevator may not be able to meet the minimum oil content the customer needs because the in-bound high oil corn is below the minimum.

Finally, the elevator manager must have enough quantity of the grain to meet the customer's needs. The risk of not having enough of a grain comes from three sources: not contracting for enough production, lack of incentives in the contract and poor yields. The main result is not having enough of a particular grain to meet demand.

Timing, another source of risk, relates to managing the logistics of handling grain. Elevator managers need to have the right quantity of the right quality of grain for the customer at the right time.

Another management challenge associated with specialty grains

involves the additional costs. We have all thought about the additional handling costs associated with specialty grains, but what about the lost income that elevator managers are used to getting from blending?

With commodity grains, elevator managers can blend grains of different grades to meet quality minimums. However, sometimes specialty grains are handled in volumes small enough to prevent effective blending, and the elevator loses that source of income. In other cases, the elevator may not be able to meet quality requirements to fill an order because there is not enough volume of grain for effecting blending. While errors in operations and inventory management are always expensive it is even more so with specialty grains and the impact on firm profitability is often larger.

Uncertainties associated with demand present another set of challenges, with new risks, for managers. Not knowing customer needs can create uncertainty about the premiums in terms of what the customer will pay for the additional value of specialty grain, the variability in the premium levels, and whether or not the premium covers IP costs or creates the desired profit margin.

## Tools at Hand

Contracts are excellent tools for managing risk and can clearly outline potential scenarios, outcomes and expectations for both the grain elevator manager and the producer or the grain elevator manager and the grain processor. Contracts provide tools for communicating what quantities are needed, what qualities are required, premium structures, production procedures and protocols and delivery time and place.

Grain quality protocols provide additional communication tools that support supply risk management. As a process for producers, (continued on page 30)

(continued from *Managing Risk* on page 29)

protocols support decision and action regarding genetic selection, equipment and input management, in-field production management, post-harvest handling and testing and monitoring of on-farm and off-farm inventory throughout the entire process.

Managing demand risks successfully require careful attention to the customer relationship. That requires learning customer needs, concerns and issues with yield, quality and price. It further requires careful targeting of customer market segments to successfully address the issues at hand.

### Balancing Price Risk Management

Remember, in specialty grain production and handling, the players in the market are concerned about both profit and risk. Everyone faces additional costs in terms of inputs such as seed, fertilizer, crop protection, equipment and often labor, as well. They manage increased risks in terms of yield, quali-

ty and price. In addition, they often must manage additional logistics in handling and delivering the grain.

Seed firms and grain handlers can help manage the risks of specialty grains successfully by hedging with

### Reducing Risk for Handlers

- Hedge using commodity markets to reduce price risk from market fluctuations
- Relationships with customers
- Awareness of the marketplace
- Flexibility in internal operations
- Relationships with producers
  - Contracts as a tool
  - Develop grain quality management protocols
  - Price risk management services for producers
- Logistics management for producers

commodity markets when appropriate, focusing on relationships with the producer, assessing market demand (which includes anticipating threats from the

competition and substitutes, and remaining flexible in working with both producers and customers.

Key to successful risk management is flexibility. Understand that even the best job of price risk management will not eliminate risk. But, those that exercise operational flexibility to deal with the unexpected have a leg up on the competition.

*Kathleen Erickson is President of Erickson Communications, Clarks Hill, Indiana; Dr. Joan Fulton is Associate Professor in Agricultural Economics, Purdue University; Dr. Frank Dooley is Professor of Agricultural Economics at Purdue University. This column is based on a distance education program on Marketing Value-Added Grains offered by Purdue University through the Cooperative Extension Service and Agricultural and Biological Engineering, Agricultural Economics, Agronomy, Animal Science, Botany & Plant Pathology and Entomology. For more information, contact Dr. Joan Fulton at [fultonj@purdue.edu](mailto:fultonj@purdue.edu).*

(continued from *Founders* on page 25) absolute dependence on animal manure to feed and nourish crops.

In 1843, a year after he patented superphosphate, Lawes appointed chemist Joseph Henry Gilbert as his scientific collaborator, and the Rothamsted Experiment Station was born as a hotbed of agricultural and scientific activity. The two men realized that providing the increasing populations with sufficient food supply would require an efficient agricultural industry and that this increased efficiency could be achieved through agricultural trials. Gilbert and Lawes worked beside one another for 57 years, laying the foundations of scientific agriculture and crop nutrition through a series of long-term field experiments, some of which are still ongoing in 2004.

Rothamsted Experimental Station is the oldest agricultural research station in the world. In 1889, Lawes ensured the continuation of the Rothamsted experiments by setting up the Lawes Agricultural Trust with 100,000 English pounds of profit from his synthesized fertilizer. Composition of the Lawes Agricultural Trust was set up to always consist of four members from

the Royal Society, two from the Royal Agricultural Society, one each from the Chemical and Linnaean Societies and the acting owner/manager of Rothamsted estate.

The station has set the standard for other centers and is currently linked with more than 40 research centers across the globe. Lawes and Gilbert carried out nine long-term experiments at the station, dubbed the Rothamsted Classical Experiments. In addition to work at the Experimental Station, Rothamsted scientists discovered and developed pyrethroid insecticides (synthetic compounds that are related to oily liquid esters with insecticidal properties). They also pioneered in the areas of virology, nematology, soil science and pesticide resistance.

Before his death on August 31, 1900, at Rothamsted, Lawes had received many honors. In 1867, the Royal Society awarded both Lawes and Gilbert a Royal Medal, with Lawes initiation to the Society given 13 years earlier in 1854. He became a fellow of the Institute of Chemistry in 1878 and was created a baronet in 1882. The Royal Society of Arts awarded Lawes its Albert medal in 1894.

Perhaps the most idyllic honor was given to Lawes by universities of academic fame. While Lawes was by nature not a successful university student in the classroom, he later received honorary degrees from Cambridge, Oxford and Edinburgh universities — high distinctions for a man who never completed his studies.

### Advertisers' Index

<b>Agriliance</b> . . . . .	<b>5</b>
<a href="http://www.agriliance.com">www.agriliance.com</a>	
<b>American Seed Trade Assn.</b> . . . . .	<b>IFC</b>
<a href="http://www.amseed.org">www.amseed.org</a>	
<b>BioDiagnostics Inc.</b> . . . . .	<b>27</b>
Ph: 715-426-0246 • <a href="http://www.biodiagnostics.net">www.biodiagnostics.net</a>	
<b>Indiana Crop Improvement Assn.</b> . . . .	<b>9</b>
Ph: 765-523-2535 • Fax: 765-523-2536 <a href="http://www.indianacrop.org">www.indianacrop.org</a>	
<b>Johnny's Selected Seeds</b> . . . . .	<b>15</b>
Ph: 800-854-2580 <a href="http://www.johnnyseeds.com">www.johnnyseeds.com</a>	
<b>Landec Ag, Inc.</b> . . . . .	<b>13</b>
Ph: 80-0241-7252 • <a href="http://www.landecag.com">www.landecag.com</a>	
<b>World Conference on Organic Seed</b> . . . . .	<b>BC</b>
<a href="http://www.organicseedconf.org">www.organicseedconf.org</a>	
<b>Tech Services, Inc.</b> . . . . .	<b>25</b>
Ph: 888-642-6322 • Fax: 260-694-6617 <a href="mailto:tsiinc@adamswells.com">tsiinc@adamswells.com</a>	
<b>World Seed Congress</b> . . . . .	<b>IBC</b>
<a href="http://www.worldseed2004.com">www.worldseed2004.com</a>	