

THE POWER OF PRICE

Severe Market Volatility, Large Price Disparities Create Temporary Shift in Farmer Buying Behavior

by Dr. W. David Downey

There is a lot of talk these days about whether or not there has been a permanent shift in farmer buying behavior ... and for good reason. Never have there been such dramatic swings in commodity prices in such a short period.

As grain prices soared, and then crashed, farmers saw their fortunes follow, depending on the timing of their decisions. Both crop and livestock farmers watched and worried as prices of their inputs gyrated, wondering what to do.

Should they buy now to lock in a price? Or should they hold off, hoping for a better deal later and take the chance their preferred products would be available when they needed them?

Meantime, their suppliers were in a like quandary. They also worried about price volatility, availability of raw materials and their own supplier's ability to deliver what they needed in time.

When and how much inventory should they order or produce? Would the demand be there? How should they price? And what will happen if they make the wrong decision?

As record market volatility continued, it has been a worst-case scenario for many input suppliers. While crop farmers are coming off a couple of pretty good years, they are suddenly nervous about their future and are reluctant to commit. Livestock and dairy farmers — feeling the pinch of

high commodity prices — are struggling to survive (and many may not).

Input manufacturers and the distribution system have been scrambling to predict demand, position themselves under uncertain circumstances and find creative ways to share the risk with others. Many agronomic retailers read all the signals, listened to the experts and locked in high-cost fertilizer to ensure an ample supply for their customers — only to be caught in an extremely painful situation when the recession brought world fertilizer prices crashing down.

The result has been chaos with lots of finger pointing. Some farmers are convinced that their suppliers are manipulating prices to become wealthy. Others, who have depended on local suppliers to provide service and information, seem to be much more sensitive to price variations in the market and switch suppliers.

Farmers who have demonstrated a great deal of loyalty in the past are now asking lots of questions. Low-margin/low-service suppliers, recognizing their opportunity, aggressively fan the flames of discontent to get new business.

BUYER SEGMENTS

Historically, studies at **Purdue University's** Center for Food and Agricultural Business have suggested that about 20% of farmers tend to be classified as economic buyers, focused more on price or getting a deal than any other factor. A third are considered relationship buyers because their most important concerns are trust and personalized attention. And the rest are described as business buyers who balance a wide range of factors (including price and the relationship) and carefully analyze where they get the best return on their money.

It is important to note that both economic and business buyers tend to manage larger operations and are responsible for a growing share of the market.

However, Purdue's most recent study of more than 2,500 farmers across the nation, concluded just before the market became so volatile, suggests that even more farmers are considering a balance of factors as they evaluate the value proposition that is best for them. This may be connected to the increasing sophistication and businesslike approach that often comes with their continued consolidation into larger farms.

Purdue studies also show evidence that farmers see fewer differences among suppliers than they once did. The reality is that new technologies, increased competitiveness and supplier consolidation at all levels has resulted in dramatic increases in product and supplier performance in the last few years.

The playing field has leveled. Suppliers have to be good to have survived. It is more difficult to create and sustain a competitive differential advantage based on unique products or services. Advantages, if they are real, are quickly copied — and improved on.

The upshot is that as products and services are perceived at near parity, price becomes a more visible and a relatively more important element in the balance of factors that discerning farmers consider.

A FUNDAMENTAL SHIFT?

My answer is no!

Price has always been an important issue to all farmers. However, market volatility has been so severe and price disparities so large that even the most relationship-oriented buyers now feel they cannot easily justify away price differences. Additionally, when farmers feel economically threatened, the price element in the value equation becomes even more significant.

As markets begin to stabilize, price differences should decrease and other factors will once again become relatively more important.

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However, as long as farmers see huge price differences for product/service bundles (including the intangibles) that they perceive as near parity, price will continue to be a powerful factor.

WHAT'S GOING ON?

What we may be experiencing is the impact of a not-so-gradual trend in farm size and sophistication magnified by economic conditions.

Many larger farm operations believe their size justifies the purchase of facilities and specialized equipment, and the hiring of their own technical specialists. So, they are no longer as dependant on their supplier. That clearly reduces a supplier's ability to add as much value or differentiate themselves...leaving price as a bigger factor in the equation. Recent farmer buying behavior studies at Purdue seem to support this trend.

Add to this the sheer economic impact on price in larger operations and the negotiating clout that larger operations bring to the table (where 10% of the larger operations often represent 90% of a supplier's business). It would be easy to conclude that price is now the dominate factor in farmer buying decisions.

But that would be a serious mistake. Purdue research clearly indicates the importance and growth of the balance segment.

The reality is that farmers consider many factors, identify their supplier short list and then negotiate aggressively with their preferred supplier — seeking the absolute best price they can get for what they want and need. What appears to be a pure price buyer to the supplier is actually a shrewd customer who knows exactly what he wants and is willing to play hard ball to get it.

Will these customers pay for service and quality? Sure, but not if they believe the bundled services do not precisely fit them. Suppliers will have to work hard to make sure that their offer closely matches the farmer's needs and communicates the value they offer.

PERCEIVED VALUE MATTERS

When it comes down to it, it always has been a value question — “Where do I get the best value for each dollar I spend.”

Value is defined as what people believe they are getting compared to what they believe it costs them to get it. Perceived benefits include a host of tangibles and intangibles that come to them as a result of a purchase.

The biggest and most dramatic element in cost is price, but price is not the only factor. The complexity of communication, time invested and location are good examples of non-price costs.

We have always recognized that real value can only be defined by the customer. Successful suppliers understand that their task is to discover and deliver what their customers will value. The difficulty, of course, is that the larger and more complex farmers become, the circumstances that determine what each values are more unique and diverse.

Each farmer is different. And larger farmers are economically important enough to justify creating unique value propositions for each individually.

CHANGING NEEDS

As times change, so will farmers' needs. They are a moving target. If larger operations want to perform

more services themselves, suppliers will have to find new ways of creating value — or do a better job demonstrating to farmers why they are better off to outsource those services.

This is not a fundamental shift in the importance of price. Wide price disparity always creates a rapid shift in buying decisions. The bigger issue is what are the changing needs of larger, more sophisticated and businesslike farmers, how do suppliers

$$\text{Value} = \frac{\text{Total Perceived Benefits (tangible and intangible)}}{\text{Total Perceived Costs (including price)}}$$

respond to those needs, and how effectively can they communicate their value.

The past year may well have taught farmers to look more closely at the value they are getting. The increasing perception of parity among suppliers does put more pressure to differentiate themselves. To be successful, suppliers will have to better understand the “unique needs” of important customers, create “unique value” for individual accounts and communicate that value more effectively than ever before. **AM**

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