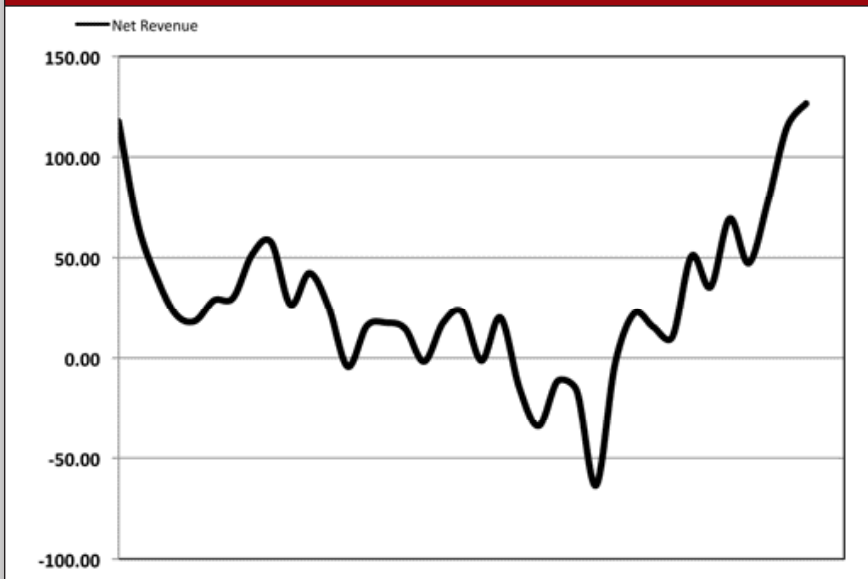
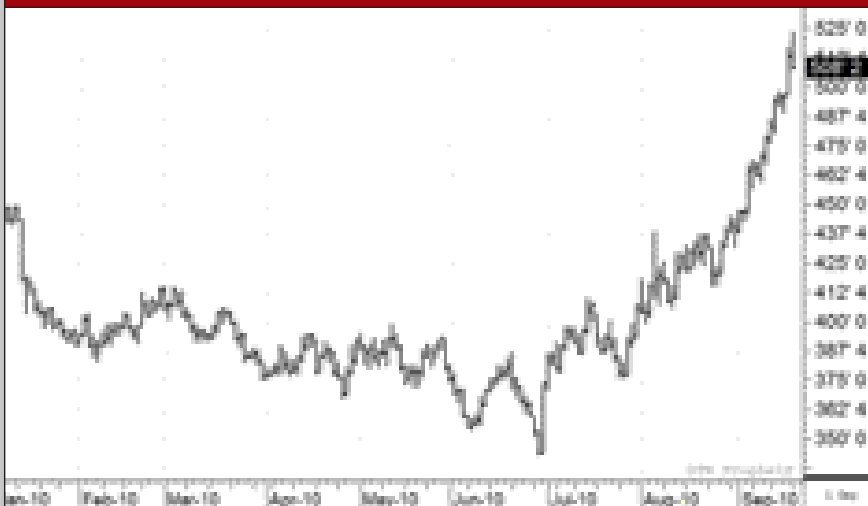


## Kluis Profit Index December 2010 Corn



## CBOT December 2010 Corn



a frustrated Minnesota farmer. This producer had a lot of corn hedges and was looking at a 90¢ under-harvest basis. I did not have a simple answer to his complex question but rather an overall approach that I use with my customers.

To begin the process, there are four basic questions that need to be answered.

### 1 What Are Your Needs?

When I first meet with a new customer, I ask a lot of questions about acreage yields, basis, storage availability, and payment schedule. The initial meeting lets me look at what the farmer needs to generate per acre, per field, or for the entire operation. I like to look not only at 2010 but also get some projections (that are, of course, subject to change) for 2011 and 2012. Successful farms have a one-year budget, a two- or three-year marketing plan, and three-, five-, and 10-year business plans.

The farmers who sit down and work on this are often the producers who have the confidence to go out and sell ahead one, two, or three years into the future when prices and profits offer a good return.

### 2 What Are Your Farm Goals?

If I meet with farmers who say their goals are to sell the top of the market, then we may not work together. If they indicate that their goal is to generate \$800 per acre in revenue for their corn and \$650 per acre for each acre of soybeans, then we will likely continue. Some farmers

## Risk Management

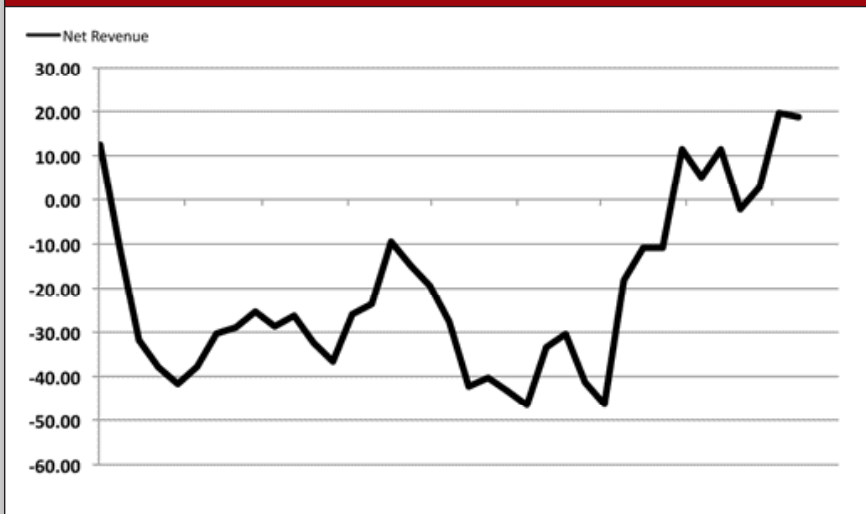
Take control of your bottom line.

How can you have a market plan that works for you when commodity funds can run prices dramatically higher than they should go and then lower than you would imagine? Like this year when corn futures dropped to \$3.20 a bushel in June and then rallied sharply higher into harvest." This was the question and comment from

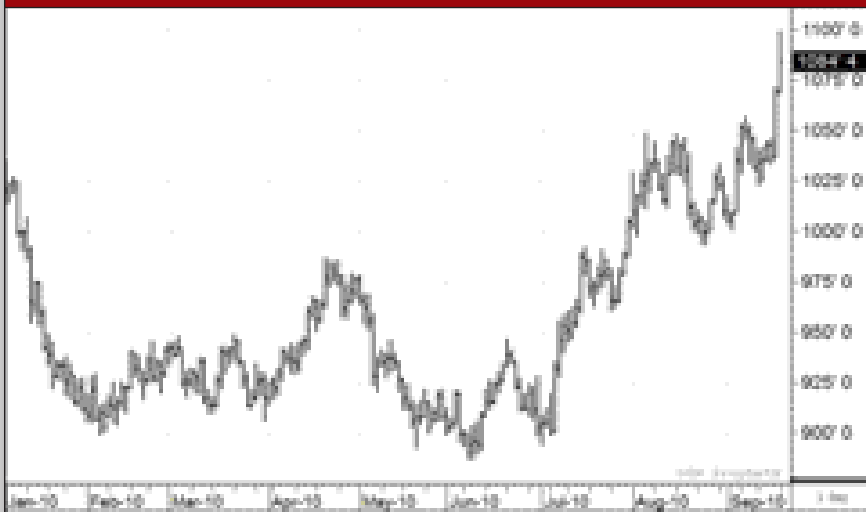
just want to generate so many total dollars of total revenue. They know this will allow them to pay off their operating note, make a living, make their land payments, and get debt paid down each year. Every farms' goal is different, and it is not always financial.

One farmer I worked with always wanted to have his grain sold and delivered by May. This was because when he was done planting corn and soybeans he could spend the summer at the lake with his grandchildren. He was a very solid, profitable, good farmer who knew his costs and had very specific income goals for each field.

## Kluis Profit Index November 2010 Beans



## CBOT November 2010 Beans



### 3 Are You Willing To Take Advantage Of Technology?

If you're not willing to use the Internet, a cell phone, or e-mail, then communicating will be slow, difficult, and inefficient. In this fast-moving market, you may not be able to receive and act on sales recommendations on a timely basis. You'll still be able to work with a marketing service, but you may not always get the best results.

### 4 What Is Your Risk Tolerance?

A young farmer who has no storage, has an operating loan at the bank, and has a lot of cash rent due in December of each

year has to have a disciplined risk-management plan. It's a much different plan for a farmer who has no operating loans and has adequate on-farm storage.

Are you willing to use futures and options? If you only sell when it's in the bin or will not use hedges or puts, you don't have as many risk-management tools to work with.

### Determine Your Approach

Once you've answered these four basic questions, you need to determine an approach. The common-sense risk-management plan I recommend is compatible for most farms. It needs to be fine-tuned to meet your individual farm, needs, goals, and stay within your risk-tolerance parameters.

My approach is to not worry about factors that I cannot control such as what the commodity funds are doing, what future USDA reports may indicate, or if there is another global financial meltdown. I will control the variables that I can in my farm business, do whatever I can to maximize yields, and monitor the new-crop futures market price levels to see when I may be able to start hedging at a profit.

Any farmer who feels like a victim of the commodity funds is usually reacting and does not have a proactive plan that is built on farm income goals.

On my farm, I have 50% of the 2010 corn hedged at \$4.40 per bushel into the March 2011 contract. I'm not concerned that the corn market is above that price level at the time I am writing this in October. The \$4.40 hedge was at an acceptable profit level. I am not greedy; I am just looking at where I will get the last 50% hedged. I hope the commodity funds rally corn futures well over \$6, so I can sell the rest of my crop at an even higher price and profit level.

### How Exactly Do You Manage Your Margins?

For the 2010 crop, putting together a plan to manage your margins is fairly easy now because you do not have a lot of known factors and less variables to work with. ➤

## Kluis 2010-12 Corn Margin Outlook

	2010	2011	2012
<b>Yield*</b>	<b>210</b>	<b>171</b>	<b>175</b>
<b>Minnesota Basis</b>	<b>-40</b>	<b>-40</b>	<b>-40</b>
<b>Revenue/A</b>	<b>\$928</b>	<b>\$713</b>	<b>\$714</b>
<b>Expense/A</b>	<b>\$559</b>	<b>\$586</b>	<b>\$615</b>
<b>Bottom Line</b>	<b>\$369</b>	<b>\$127</b>	<b>\$ 99</b>

\* Crop is excellent this year. Will use 5-year average yield in 2011 and a 2% increase in 2012.

Here are three simple steps you can take today to see how you are doing with your 2010 crop margins.

**Step 1.** Your acreage and yields are known, so you should be able to know your total production. By the time you are reading this, you should have your 2010 crop put away so you will know how many bushels you have to work with. You know where it is stored, how much is hedged, and the approximate total value of your 2010 crop.

**Step 2.** Your 2010 crop expenses should be known – except for the last of the 2010 dryer gas, fuel, and repairs you pay by the end of the year. Add them all up so you know what your total expenses are going to be for 2010.

**Step 3:** By computing your crops' total value (Step 1) and then deducting your expenses (Step 2), you should have a good idea of your 2010 bottom line.

### 4 Key Variables For Grain Farmers

There are four key variables that have a huge impact on your income as you plan ahead into 2011.

**1. Yields:** This was a challenging year, with a disappointing end after a great start. For those of you with trendline or better yields, the 2010 crop is likely a profitable crop. If you are in an area with corn yields that are only 50% to 70% of your five-year average, it is difficult to project any bottom-line profits on the 2010 crop.

**2. Input Expenses:** Grain and fertilizer inputs have jumped since the major lows in June 2010. If you were able to get your

fertilizer bought ahead early for the 2011 crop, you have made the right decision. The right time to book 2011 fuel is still to be determined.

**3. Crop Sales Price:** Some farmers ended up selling a lot of cash corn and soybeans in late June and early July when they needed the money. Now, even with the fall rally, 2010 is stacking up to be a challenge. Of all the variables, where you sold the 2009 cash crop and where you put on the 2010 hedges are what will make the largest bottom-line difference.

My subscribers should have at least 50% of the 2010 crop sold on hedges from earlier this year. These hedges were locking in at least \$90 per acre of corn bottom-line profit and \$50 per acre for soybeans.

**4. Merchandising Decisions:** If you have on-farm storage and are able to roll hedges ahead into the March-July 2011 time period, you can earn an additional 30¢ to 40¢ per bushel. The ability to capture the carrying charge and basis appreciation can add on \$50 to \$80 per acre to your 2010 corn bottom line. If you understand merchandising and making the right decisions, you can double your corn bottom line.

### How Will You Know When To Sell?

How did I make the recommendations about when to sell the cash crop and put on new-crop hedges?

A lot of the decisions on when to hedge were made by looking at the Kluis Profit Index (KPI) that I maintain for corn and soybeans on my website each day. This Index is my projection of a typical corn and soybean farm's per-acre profit that changes with the market each day. The KPI assumes average yields, new-crop futures prices, and new-crop basis.

The top chart on page 8 shows corn profits going from over \$120 per acre in early January 2010 to a \$60-per-acre loss by early July. The top chart on page 9 shows soybean profits going up from a \$10-per-acre profit in early January 2010, dropping to a loss of \$45 per acre by July before rallying back to a \$70-per-acre profit at harvest. The initial draft for the 2011 KPI shows December 2011 corn futures at \$4 per bushel offer a break-even for farmers; the November 2011 soybean futures show a projected break-even when futures are at \$9.88.

The profit outlook for corn and soybean farmers is challenging as I look at trying to lock in margins for 2011. For 2011,

## Kluis 2010-12 Soybean Margin Outlook

	2010	2011	2012
<b>Yield*</b>	<b>62</b>	<b>46</b>	<b>47</b>
<b>Minnesota Basis</b>	<b>-40</b>	<b>-40</b>	<b>-40</b>
<b>Revenue/A</b>	<b>\$650</b>	<b>\$496</b>	<b>\$508</b>
<b>Expense/A</b>	<b>\$415</b>	<b>\$436</b>	<b>\$460</b>
<b>Bottom Line</b>	<b>\$235</b>	<b>\$ 60</b>	<b>\$ 48</b>

**\* Crop is excellent this year. Will use 5-year average yield in 2011 and a 2% increase in 2012.**

I am using a 2% increase of my five-year average yields, basis levels the same as 2010, a 5% increase in input expenses, and a 5% increase in land costs. The margins are very tight.

For 2011, here are some initial suggestions for you if you have a stable land base and known land costs for next year.

**Corn:** Have your 2011 fertilizer locked in by early July 2010. Most farmers have 20% (of insured bushels) of the 2011 crop hedged with enough dollars sold ahead to cover the 2011 crop in puts that have been locked in. The fertilizer-to-corn futures ratio was at a good level to lock in both sides. If December 2011 corn rallies high enough to take the 2011 KPI up to \$100 per acre, lock in 40% of your insured bushels.

**Soybeans:** With November 2011 soybean futures at \$10.68, have 20% of your insured bushels hedged. The profit goal is to get up to 40% to 60% of your insured bushels locked in if you can hedge ahead a \$100-per-acre return. That is a long way away, but if commodity funds want to run soybean prices higher to a good profit level, sell it to them.

**Wheat:** With new-crop 2011 wheat futures over \$7 per bushel, have 50% of your 2011 crop hedged. Consider getting the rest protected with puts. The outlook is bullish for wheat, but all indications are there will be a lot more wheat in the world by June-July 2011.

### Projecting A Profit For 2012

Trying to project a profit for 2012 is even more of a challenge. Right now when I use an additional 2% increase in

my five-year average yield, another 5% increase in operating and land costs, the 2012 December corn and November soybean futures do not offer an acceptable return.

I plan to talk with my suppliers about when the fall 2011 fertilizer and fuel prices will be available, and I will monitor the 2012 November soybean and December corn futures prices. But if I'm not able to know my 2012 inputs, it is impossible to know what price I need to sell ahead to lock in a profit for 2012.

I use a proprietary software program called Profit Snapshot to see where my Minnesota farm is (see tables on pages 10 and 11). My three-year look-ahead for corn is based on my current projections for expenses and the price levels I'm at for 2011 and 2012 futures. I update the

expense side quarterly; the estimate on income change each day depending on the closing futures price.

Looking ahead to 2011 and 2012, the margins are less as I project average yields, a 2% increase in yields, and a 5% increase in costs. I have the 2011 inputs bought and will be willing to get 30% to 40% of the 2011 crop hedged if I can lock in \$100 per acre on my corn and \$70 or more on soybeans.

I know farmers and a lot of money managers are bullish on agriculture, but with the current global economic problems still unfolding, I will feel better having some profits locked in for 2011, after having a great year in 2010.

With all this information, you still have to decide what to do. Here are my suggestions for an action plan:

1. Get your 2010 crop sold the best you can.
2. Get your 2011 inputs locked in.
3. Get 30% to 40% of your 2011 crop hedged ahead of when you can get a \$100-per-acre return.
4. Monitor the cost and availability of fertilizer and fuel for delivery in the fall of 2011. □

### Al Kluis

**Al Kluis has been a commodity trader and adviser since 1974. To learn more about managing your margins, plan to participate in a free online webinar Tuesday, December 14, 8:00 p.m. CDT. Register at [alkluis.com](http://alkluis.com). Kluis Commodities 901 - 12 Oaks Center Drive, Suite 907 Wayzata, MN 55391 888/345-2855 | [al@alkluis.com](mailto:al@alkluis.com)**

