Risky Business

Panelists share experience, advice for managing risk in cattle feeding.

*by **Lyndee Stabel** and **Steve Suther,***
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►On the southwest panel, the banker role was filled by W. Ashley Allen (right), Amarillo's Bank of America Merrill Lynch market president. Brent Manwarren (center), risk manager at Poky Feeders, Scott City, Kan., rounded it out with James Herring (left) of Friona Industries, Amarillo, this year's FQF Industry Achievement Award honoree.

Risk in cattle feeding skyrocketed with costs and prices in recent years. Still volatile but not bullish, the market demands greater risk management than ever, according to panelists at the August Feeding Quality Forum (FQF) at La Vista, Neb., and Garden City, Kan.

In Nebraska, advice came from commodity brokers Doug Deets of Buchanan & Co., Manhattan, Kan., and Scott Mueller of Samson Commodities, Columbus, Neb. Marshall Hansen, of Farm Credit Services of America (FCSA), Omaha, provided a banker's view.

On the southwest panel, that role was filled by W. Ashley Allen, Amarillo's Bank of America Merrill Lynch market president. Brent Manwarren, risk manager at Poky Feeders, Scott City, Kan., rounded it out with James Herring of Friona Industries, Amarillo, this year's FQF Industry Achievement Award honoree.

Hedging in the futures market is a primary means of allaying risk in cattle feeding. Hanson said 90% of FCSA feedlot customers from the Dakotas to Texas hedge something: "It could be energy, feed, interest rates, live cattle, feeders …"

Mueller looks at four main categories, from buying and selling commodities to weather and the unique "people" factors associated with every customer.

On the Kansas panel, Herring noted 13 elements of risk on the purchase or sales side that can be hedged. In the futures market, that means margin calls.

Allen said a 40,000-head feedyard needs a $40 million line of credit these days, partly because of the need to meet the obligations of hedging.

"The futures market can chew up enormous amounts of money when it goes against you, so you want to make sure your banker understands what you are doing," he said.

Manwarren, who handles hedging accounts for customers, said Step 1 is to learn about their cattle, from genetics to management. That allows for more accurate estimates of performance and profit potential.

A conservative approach adds cushioning. He never figures potential grid premiums into breakevens but lets them offset occasions of bad weather or other unforeseen issues that crop up. He also offers to handle the inevitable.

"How does it feel when you get those margin calls?" Manwarren asked. "When we are the ones taking those calls, you don't have to write a check, so you don't feel that pain. When we get to the end, if we've done our job and fed the cattle efficiently, what you see on your end is a good return on your capital."

Leave emotion at home

Deets said among the top 10 cattle-feeding companies, there are 10 distinct risk-management strategies, but all find ways to separate emotion from business. Those with less experience soon learn the importance of discipline.

"You have to have goals and communicate about the market," he said. "When the key price arrives in the market, it drives me crazy to find out a customer sold two weeks earlier."

Hanson injected, "You have to understand it as business. When you come off of a lost opportunity and decide 'I'm never going to do that again,' that's probably when you need hedging the most."

The panel discussions in August noted a very wide spread between feeders and finished cattle.

"It's the biggest disconnect I have ever seen in my career," Deets said of the last 40 years, surmising a major shift. "This is starting out as the most aggressive expansion since the 1980s, and nobody gets how the cycle works now because we have been in liquidation since then."

Mueller said nontraditional avenues of risk management can take in "land ownership, cropping systems, home-grown labor, government farm programs and creative ways of working with people."

Herring said, besides extensive hedging, Friona Industries manages risk through its business model of partnering with Cargill in a quality-focused supply chain.

"Thank goodness someone allowed us to value the kind of pound rather than just the pound. And we started seeing that we could separate ourselves by valuing the animal by the individual cuts we were able to create," Herring said.

An accumulated database lets the company go back to sources that perform best in the pen and on the rail. Over time, the data led Friona to fill nearly 75% of its pen space with black cattle.

"When you're feeding cattle in this tough environment," Herring said, "you want to feed something that gives you the best chance for some of those premiums." He credited 35 years of the *Certified Angus Beef*® (CAB®) brand for having changed "not only eating quality, but genetic quality and production practices."

That demand signal from Friona is strong, Herring said. If cattle come through in good health with top-notch performance and carcass quality, "You are going to have to tear our arm off to keep us from buying them next year."

Panelists at both locations also shared experiences, in hopes that feeders could learn without having to do all the "trial and error" themselves.

Change is the constant, they agreed.

"Bear markets lead to bull markets and vice versa," Deets said. "We're just one weather event away from higher grain prices now."

The Forum is co-sponsored by Roto-Mix, Purina Mills, Micronutrients, Zoetis, *Feedlot* magazine and Certified Angus Beef LLC.

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Editor's Note: *Steve Suther is the director of industry information and Lyndee Stabel is a freelance writer for Certified Angus Beef LLC.*