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## **Developing a Dairy Marketing Plan**

by

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I teach a dairy marketing course at Cornell University. One topic thread that is woven throughout the semester is that although price risk in dairy markets is real, it can be managed. The only way to ultimately make good decisions about the adequacy of a milk price and the strategy employed to protect it is to remove emotions from the decision-making process. This is best done by the development and implementation of a marketing plan.

Creating a marketing plan does not need to be a difficult process. However, the process should generate a physical document that is your personal road map to price risk management. There is not “one recipe” for such a document, but there are several items that every good marketing plan should address. For instance, how vulnerable is your operation to the big price swings that we have seen in the past decade. A couple of numbers such as a debt-to-asset ratio and a debt coverage ratio will help you understand your vulnerability. Another assessment to be made is your personal tolerance to risk. If your business is quite solvent and you have a high tolerance to risk, a perfectly acceptable decision may be to just take what the cash market gives you. If either your business or your personality can’t handle large price swings, then your marketing plan needs to be a bit more ambitious.

A marketing plan must also contain an understanding of your cash costs of production. This is often called your operating costs and it differs from the total costs of production, which further includes values for depreciation, returns to equity in your business and a return to your labor and management. Those costs have to be covered in the long-run, but in the short-run, it may make sense to produce milk at a milk price that doesn't allow you to replace capital items. However, locking in a milk price that is less than your cash costs of production never makes sense. You should be willing to gamble that the cash market may recover by the time you actually sell your milk rather than to assure yourself a loss on every hundredweight that you produce.

I suggest that you choose three price goals as triggers for action. The lowest price goal is your operating costs of production. Beyond mere business survival, a second reasonable price goal should include an adequate family living withdrawal, money for capital replacement, etc. A final "I want it all" price goal should adequately fund any other reasonable items such as off-farm retirement investments, college funds for your children, etc. With these goals in mind, you can begin the next step in the plan.

A futures market or a fixed price forward contract will not directly relate to your price goals. The Chicago Mercantile Exchange (CME) has futures contracts and options for a class III or class IV milk price but you don't receive either of those class prices as your milk check. Some forward contracts have been offered as blend price contracts, but very few producers sell milk at the standardized component values of a blend price and most receive some level of premiums. You need to understand how your milk price relates to a futures market or fixed price forward contract. That relationship is called a "basis". A simple comparison of your milk checks to the contract benchmark (class or blend prices) for the past couple of years will provide the mapping of your price goals to a needed contract price.

The final piece of a plan details what you will do when one of the triggers is met. Here it helps if you have some idea of how the market opinion is moving. If the CME class III price for September milk meets your highest price goal but has been moving upward, then you may want to purchase a put option which places a floor under the price but allows for additional upward movement. If the CME price meets your highest price

goal but has been falling, you may want to sell a futures contract or consider a fixed price forward contract as a less expensive means of retaining the price goal. There are many different strategies that can be employed under different circumstances.

Finally, you should think about evaluating your marketing plan. After it has been in place for several months, ask yourself if it is performing as you would like it to or whether it needs to be modified. You should also consider how much time to spend on marketing your product. It will be more difficult to reach your price goals if you don't spend a good deal of time focusing on ways to lower or at least maintain your operating costs through good management practices.

Some, or perhaps many, of these marketing concepts may be new to you. As one producer told me, they may be confusing at first but it's not rocket science! Perhaps one of the best ways to tackle something like a marketing plan is to join a marketing club. There are several that are being started in the state, and we are helping to support the learning process with materials and guest speakers. Acquiring this type of knowledge may be best done in a group atmosphere. Ask your local Cooperative Extension office about forming or joining such a group or visit [http://hortmgt.aem.cornell.edu/risk/newsletters/marketing\\_clubs.pdf](http://hortmgt.aem.cornell.edu/risk/newsletters/marketing_clubs.pdf) for additional information about marketing clubs.

**"Smart Marketing"** is a monthly marketing newsletter for extension publication in local newsletters and for placement in local media. It reviews the elements critical to successful marketing in the food and agricultural industry. Articles are written by faculty members in the Department of Applied Economics and Management at Cornell University

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