

It is two years since the wheat industry was deregulated and timely to view where the industry is at, two seasons down the track. Whilst the papers were filled with the mixed viewpoints of those supporting and opposing the reforms, a review of the effect of these changes is well due.

As many primary producers across the state are taking off a harvest that will bring mixed results in terms of price and yield, there is one group of farmers that will be celebrating another good year of very high prices achieved through a marketing plan that has been written and strategised over 30 years. The proponent of this plan promised that a deregulated market would provide for much better prices for farmers and to date, this has occurred for followers of the theory. Prices will still go low regardless of deregulation as the wheat market is a world market, but it is how this is managed by farmers that is the key. Surprisingly this marketing formula has been developed by a person who knows very little about the technical side of farming, but has scrutinised some of the practices of the industry and advises clients that much of the thinking of the industry should be questioned and challenged. David Burton is the Managing Director of Commodity Hedging Co.Pty.Ltd. David experience in commodities goes way back to 1983 when he started with an Asian futures broker based in Brisbane. In 1987 he started a job with the Cotton marketing board and work there until he started his business in 1990. The cotton industry was one of the first to be deregulated in Australia and David's job was to hedge currency and futures as well as educate growers on risk management.

The methods that David uses are nearly impossible to learn as they involve the complex cycle timing of the greatest forecaster of all time W.D.Gann, which took David twelve years to decode. Having dealt with farmers businesses and hedging since 1987 David was able to develop a hedging program combined with time cycles, weather forecasting and strategies to cut down the risk to a very small amount. When other advisers and farmers lost a combined \$100 million in Western Australia alone in 2007, David clients received \$600 a tonne with not a cent lost. Why? Because he forecast with the use of time cycles the high twelve years in advance in a public magazine in July 1996 called "Your trading edge". No one ever makes public forecasts in writing, let alone that far in advance. They can't do it.

David has made many public forecasts in advance as TIME CYCLES repeat and human nature doesn't change.

The enthusiasm of growers experiencing the success of this marketing plan, are keen to tell the story and encourage others to explore some new thinking on how they are marketing their grain in this new environment. The momentum

is gathering to have fellow farmers create a economically sound and vibrant industry, where we have increasing control over prices achieved and more power and creativity in our businesses. Farmers are notorious for wanting to distribute information that benefits another and some better ideas on grain marketing in the current climate would be welcomed.

HISTORY

The farming industry can be described as one where collaboration has been the strength of what has been achieved, but likely, this same feature may have been its weakness also. When one questions how the wheat industry came into being a monopolized entity, and whether this worked, a review of archives reveals that as far back as 1915, an Australian Wheat Board set up a pooling scheme to assist growers. War time measures were beneficial to growers because they were freed from the dominance of wheat merchants and the existence and impact of price and shipping cartels whose collusive actions depressed prices. Growers didn't have the communication devices available to them that exist today. Additionally in the early 30s, the impact of the Great depression, Govt intervention and following a period of rapid expansion in the industry, world wheat prices declined significantly and the industry entered a serious economic slump. Through extreme times, measures such as those adopted were necessary. From WW 1 to 1984 comprehensive wheat marketing legislation was enacted. Basically, this removed producers competition in the output market. Whilst the industry focussed on incredible improvements in technological innovation into improving yield and methods to produce a quality product, the prices achieved were determined by the expertise of the wheat board of the time. There was no perceived need for farmers to understand the commodity markets that determined their price, it seemed. One wonders if in recent times, the regulation empowered farmers in any way. Were the prices achieved representative of the opportunity available through the expertise of highly paid marketing people and executives, or did the limiting legislation and costs diminish the returns? Did it create farmers that had dynamic business plans or did it put them into a plethora of sameness and eventual reliance on costly agribusiness consultancy to give them direction and assistance with their business?

Wheat farmers have now entered a new era whereby they have opportunity to control their own marketing. Attendance at marketing information events, growers are relayed a multitude of information on destination markets and international consumption projections and trends whilst it is questionable that any of this is relevant to the reality of what makes up the wheat price. For clients of Commodity Hedging Company, the factors to concentrate on

primarily are the three components of price. Futures, currency and basis. The CBOT futures market was established in 1848 and was set up to ensure that there were buyers and sellers for commodities. Currency has been able to have been hedged since 1983, so up until two years ago farmers have been able to achieve 2/3 of their own marketing. Unfortunately the single desk was the only means of controlling basis up until two years ago. Now we have more merchants in the marketplace which means more competition on basis.

POOLS

David Burton explains that pools have never worked in any industry in Australia, price wise and in actuality are way behind what should have been achieved with good marketing.

Year	Average Marketing	AWB Pool
1991	307	132
1992	213	200
1993	217	165
1994	254	174
1995	301	237
1996	344	260
1997	280	212
1998	232	197
1999	200	186
2000	184	195
2001	192	232
2002	284	261
2003	316	265
2004	482	215
2005	358	197
2006	424	265
2007	830	422
2008	976	325
2009	698	258

Why would grain companies want growers to participate in their pools? The volumes achieved helps to divide the costs of running their businesses. When you have low volume years as in the case of drought years, the costs become huge as growers saw in 2006. For example, the salary of a CEO might be \$500 000. If you divide that into a 20 million tonne pool, it is 40c per tonne, but into a 1 million tonne pool it is \$2 per tonne to pay them. There are many costs that publicly listed companies may need to cover. Some of these are for restaurants, first class travel, accommodation, cars, phones, advertising, football tickets or box seats at sporting events. It is easy to see that these costs would be better divided up in high volume pools. The legal costs and practices of the AWB were absorbed through pool returns. The estimates provided at the beginning of the season often coincide with the final payout of

a previous pool. Growers need to review that the pool price at the end of pool time frames can last up to two years and is the cash price plus interest over time. Understand that the 'estimate' is by no means a guarantee of price. When farmers really delve into their business planning and look at understanding their risks, then the idea of participating in a scheme that is unsecured such as pools would likely cause them to question or look for greater guarantees for themselves. Davids comments are "Pool are for fools" and "Money evaporates from pools, as water does".

ESTIMATED POOL PRICE OF \$200

Est Production	% hedge	% yield increase	price increases to	Final price
2000000	100	15	250	\$207
2000000	100	15	300	\$213
2000000	100	15	350	\$220
2000000	100	15	400	\$226
2000000	75	20	250	\$208
2000000	75	20	300	\$217
2000000	75	20	350	\$225
2000000	75	20	400	\$233
2000000	50	25	250	\$210
2000000	50	25	300	\$220
2000000	50	25	350	\$230
2000000	50	25	400	\$240

Est Production	% hedge	% yield increase	price decreases to	Final price
2000000	100	15	175	\$197
2000000	100	15	150	\$193
2000000	100	15	125	\$190
2000000	100	15	100	\$187
2000000	75	20	175	\$196
2000000	75	20	150	\$192
2000000	75	20	125	\$188
2000000	75	20	100	\$183
2000000	50	25	175	\$195
2000000	50	25	150	\$190
2000000	50	25	125	\$185
2000000	50	25	100	\$180

Est Production	% hedge	% yield decrease	price increases to	Final price
2000000	100	15	250	\$191
2000000	100	15	300	\$182
2000000	100	15	350	\$174
2000000	100	15	400	\$165
2000000	75	20	250	\$188

2000000	75	20	300	\$175
2000000	75	20	350	\$163
2000000	75	20	400	\$150
2000000	50	25	250	\$183
2000000	50	25	300	\$167
2000000	50	25	350	\$150
2000000	50	25	400	\$133
Est	%	% yield	price decreases	
Production	hedge	decrease	to	Final price
2000000	100	15	175	\$204
2000000	100	15	150	\$193
2000000	100	15	125	\$190
2000000	100	15	100	\$187
2000000	75	20	175	\$196
2000000	75	20	150	\$192
2000000	75	20	125	\$188
2000000	75	20	100	\$183
2000000	50	25	175	\$195
2000000	50	25	150	\$190
2000000	50	25	125	\$185
2000000	50	25	100	\$180

HEDGING

The great prices achieved by growers in the three years mentioned have been through the use of various hedging tools available to wheat growers only. An enviable and unique position available which is greatly underutilised, it seems. The use of swaps are paramount in the programme. Making use of the time when high prices occur on the futures market and low currency and locking these in to the highest percentages allowable to the furthest date (3 years). There is no production risk with swaps and with close monitoring of your position report, a close out of the position can occur at any time. Davids approach is, that when high prices occur and a profit is assured, the hedging percentage is high. Getting paid cash in the shortest time negotiable for contracts and depositing proceeds into their own accounts sees growers making more money from astute business management than languishing over the extended payout process of pools. The business transactions are much more transparent and easily accounted for and checked over. In addition to swaps - options, futures and currency contracts may be employed. Growers have never been the recipients of high prices as the AWB had a limited forward hedging programme. So, in actuality, no marketing has ever been

done for farmers. This is obvious in the prices recorded. Do farmers really need advice from advisors with university degrees to go into a pool? When the wheat price is high, merchant reps have been heard to have said “don’t hedge” or “we have five years of these high prices”. They create a position in the market for themselves. The market drops, the news is bad and they then tell you to sell as they cannot “foresee any lift in demand” or “cannot sell wheat on the international market for more than...\$xx - nobody wants it” They then buy back their positions by buying grain off you. They are in business also. The advantage of doing your own derivatives is when it is close to harvest, you can decide who has the best credit rating and best basis. Some have credit ratings as bad as –BBB which means the cost of funding is probably higher than other merchants. Farmers need to know about and calculate these risks.

STORAGE

Storage of grain this year is a topic well versed in these pages of recent times as growers seek to address their limited margins and explore how they can add value or recover some costs. It seems growers are never hesitant to spend more money. David Burton points out to clients that when you store a commodity you become a cash speculator, which means you are making a forecast that the price of the commodity will go up. Some farmers stored in 2007 and 2008 when record prices were available. If you don’t sell when the price is high, when will you sell? The problem of storage is exacerbated because if you haven’t sold last year’s crop and store, it’s unlikely you would forward sell for future years. Therefore you have lost a profit potential as well. History shows the price stays lower for longer periods than it does high, so storage is working against you. If you wanted to speculate, you should have sold for cash and bought call options if you thought the price was going up. You would be financially better off as the interest you received would pay for the call option. David suggests that growers nominate a date in the season after harvest when they sell for cash, win, lose or draw and concentrate on the new season planning. If price is below production at the start of planting next year, growers should consider not planting. When a grower grows a crop and hasn’t forward sold he becomes a cash speculator, and hopes that prices go up. This is very dangerous to grow because the prices could stay down for another year or years depending on the economic cycle we are in. The other thing that makes it worse is that if you have an oversupply due to weakened demand and large production and keep growing you are actually adding to your own demise because you add more grain to world ending stocks. If

everyone didn't grow the price would go up if you were to do this at the same time demand picks up. So then, how do you take advantage of a move up in the market without growing? You would hedge against a price rise by buying futures or call options. You would also save your machinery for high price years, scale back on labour costs, and take the opportunity to rest your soils and yourself. There would be many a farmer this year that may be thinking that it would have been wiser to not grow this past year, given the outcome.

The views David Burton toward the amount of debt in the farming sector is one of awakening. Where risks are plenty in the form of weather, geographical, economic, and market to name a few, the amount of debt adds one more in the form of interest rate exposure. With currently \$58 billion worth of debt, David warns of the cost of actually paying off this debt, and the phenomenal amount needed to cover the taxation liability in profitable years plus the principle owed. The mindset not to pay tax by spending money on overvalued products is a burdening strategy. Farmers in credit are in a position where they are not a "servant to the lender" as stated in the bible and even Groucho Marx warned that "banks may lend you an umbrella when the sun is shining and then want it back when it's raining". A credit position allows for greater creativity and options in determining the price you can achieve for your future commodity market. In years where there is no guarantee of a good price, the prospect of not growing at all is then available to you. If you are not presenting a budget to the bank to satisfy their lending criteria, then you have no one to answer to in respect of your intentions in your business. Growers really need to be aware that the banks' lending criteria can and does change as seen in the latest credit crisis, and their terms may become very changeable as the economy changes, e.g. from low to high interest rates.

Budget and Position report Tables (pg 6)

So how are farmers hedging successfully? The story of a number of businesses who met David early in 2008 is similar to that of Wagin farmers, Scott & Joy Angwin.

"I met David at a workshop in Kulin in March 2008, talked to him at Woolorama, and decided instantly that we needed to use his grain marketing advice. By the 17th of March, we commenced three years of forward marketing for wheat and canola." Joy says.

“He directed us to scrutinise our business planning and use the tools available to us in the short term to manage our grain pricing and now for our future we are looking to set up better arrangements with the businesses and banks of our choosing.

In 2008, we averaged a wheat price of \$520 per tonne. (1225 tonnes) and canola price of \$670 /T (500 tonnes) This was done through selling swaps, buying put options, and pricing grain at the correct time. We produced 2500 tonne of barley which was all priced and sold before and just after harvest. With 1300 tonne of grain storage available to us, it was tempting to hold onto some grain, but we didnt, and it was the right decision.

David has guided us very specifically with managing the risks of fluctuating input costs and suggested how we could ‘hedge’ our input costs also. Our normal barley planting programme is over 500 hectares. In April 2009 , David advised that it was risky to grow barley in the current price climate and as we couldn’t hedge it, we scaled planting back to 60ha. The prices are currently at cost of production.

I believe we are taking significant steps to gain knowledge in understanding what the opportunities and risks are with grain marketing. David Burton gives advice and explanation but clients manage the execution of all the dealing. Clients are understanding the risks of the decisions they make, and have strategies planned going forward. We need to be able to utilise all aspects of the hedging facilities available to all businesses. Managing a fluctuating foreign exchange rate is integral to managing the price we receive.

In choosing a commodity advisor, it would be prudent to really explore the success of the advisor. Have they traded the commodity markets themselves or are they working for wages ? is it the only business they conduct? What is their trading record? It will soon tell you if they are the person to adopt to assist you in your business. Successful people are usually open and honest and happy to prove their worth to you. It is imperative that farmers carefully monitor their hedged positions. In 2007 the industry lost over \$100 million because farmers didn’t cut positions when they needed to. Advisors obviously weren’t advising this, or keeping position reports for their clients so they could see how much of a losing position they were in as yield potential and price changed. They were unwise to sell forward in cash because you can never buy your position back. With swaps, there is only your market loss. Not one of Davids clients lost money in 2007. The real cost of this loss in 2007 is similar to the losses incurred over the years that no marketing has been done for farmers. An example in dollar terms is

Approximately \$150 x 12 million tonnes x 30 years is the figure that WA has lost in income to rural communities, and most of us have a sense of that loss when we look around us. Most people have left and so have our youth. When you times this figure by nine then that is what our economy overall has lost by the inadequate marketing. Only people who made money in the wheat industry in the latter days of the single desk were the highly salaried people of the AWB, and they wouldn't have survived just on marketing in their own business.

For the rural industry to progress, in the long term vast improvements are required when hedging commodities. Billions of dollars are lost each year due to low prices at harvest time. New methods and ideas are long overdue in the wheat industry. Seeking out new people who have this knowledge is vital.

David has been trading and studying the methods of WD Gann since 1983. David also is the only person teaching the authentic methods of W.D.Gann in the world and developed his **School of Gann** in 2002, Go to www.schoolofgann.com.

WD Gann was the greatest trader and forecaster of all time (1878-1955). He began by studying the basic principles of price patterns and philosophy on how to accumulate wealth, and keep it. After becoming successful, he wanted to know why and how markets and numbers repeated under certain time cycles. This led to further studies of ancient geometry and cycles. David is recognised as the leading expert in the world on the methods of WD Gann. His public forecasts compiled are an impressive folio that dictates that he knows about markets. Unlike most advisors David actually trades his own account, makes decisions and acts on his own investments (which also include rare coins, investment artwork and other investment vehicles) based on his knowledge of the Master Time cycles. He has also managed his own company since 1990, and therefore understands the risks associated in business. Davids approach is very conservative, and he prides himself with always being prepared for the unexpected. All service businesses that farmers employ cost money, but the return on the investment for Davids consultancy has been incalculable – clients asking how, if they pay more, can they extract more of this unique opportunity.

Nuffield scholar and client, Simon Tiller has said that “there are few ways in which you can really make a difference, and marketing grain GET DETAIL

Farming is a great industry and the potential for profit is enormous, but farmers cannot afford to wait for food shortages and increasing populations to

make their work worthwhile – there are too many other entrepreneurs seeing the opportunities and taking them before the price reward gets to them – they need to create their price through proven advice and very good business management.