By Diana Klemme

Discounting your profits?

Once again we are with Mike, the general manager of our mythical multistation grain cooperative located somewhere in the Western Corn Belt. Today, Mike is discussing the company's P&L with his accountant and the conversation is not going well. Nevertheless, Mike's temporary misfortune sheds some much-needed light on how discounts can rob you of profits and productivity, and FEED & GRAIN *examines ways to minimize the impact discounts have on your bottom line.*

Mike sits fuming in his office, looking at the bottom line of the monthly P&L. He hasn't looked at the details but his anger is building.

"What happened last month, Alan?" says Mike to Alan, the company accountant. "These corn and soybean numbers are terrible — I can't imagine what caused the losses. I know the basis weakened and we should show a small loss on our company-owned inventory, and on some forward contracts, but we had already estimated that for the bank. This is much bigger!"

Alan takes a deep breath; "I think you'll find most of the answers on page three Mike, most of the problem is in discounts."

"No way," Mike replies, "not possible"; but slowly he turns the pages one at a time looking at each category. Sure enough, though, there it is. "How could we possibly take that much in discounts?" he ponders aloud.

"I wondered the same thing, Mike, so we looked through our settlements to verify discounts," Alan notes. "I started with corn because we shipped over 1.5 million bushels last month and a lot of the cars that went to the ethanol plant graded 16% moisture or slightly over.

"The ethanol plant discounts 9¢ per bushel for 16.1-16.5% plus 2% shrink. On $6 corn the shrink alone costs 12¢. We took a 21¢ hit on all those wet bushels. But there's worse news," he says sheepishly. "I discovered that a lot of the soybeans shipped out of the Greentown elevator tested just over 13% on moisture and were discounted 1 ½% of contract price.

"Don't ask me how they managed to test over 13% — that's a different story," Alan continues. "We priced those beans in March — the cash price was over $15 so that moisture discount cost us over 20¢ per bushel. To add insult to injury, about 25% of the beans also tested 1 to 1.5% FM, which cost us a bundle in shrink as well."

The bad news kept on coming for Mike, as Alan recounts his concerns that the locations that were shipping don't show equivalent inbound moisture discounts from prior months.

By now Mike is furious. He's worked hard to tighten controls, and even implemented training sessions on proper handling of ground piles. He thought grain quality issues were well under control and has been spending most of his time on finance issues and meeting with bankers, and monitoring companywide risk. Keeping sufficient working capital and credit lines has been a full-time job!

But Mike takes a deep breath — getting mad won't solve the problem. Instead he calls the operations superintendent into the office.

"Jerry, have I got a deal for you!" he says with a purposeful, wry grin. "I need you to upgrade our program on grain handling and quality." Mike shows Jerry the "discounts" section of the P&L. "Clearly my efforts haven't been enough and I'm counting on you to get us back on track."

Mike knows his business can't afford to take shrink or discounts as percent of price on grain when corn's over $6 and soybeans are $12 or higher, and wheat's over $8. After careful consideration Mike lays out the following items on Jerry's "to do" list:

Meet with all our employees who grade inbound grain and re-assess their skills and knowledge. If they need training, arrange for a qualified inspector to hold a class for us. Clarify that we expect inbound grain to be graded properly and marked on the tickets. No special deals or "hair-cutting" grades. It isn't fair to reward farmers who bring us off-grade grain at the expense of other patrons.

Check their grading equipment. Are moisture meters calibrated properly? Do they have the proper pans for screening foreign material? I bet we haven't checked those in years?!

Get our merchandising department, our station managers and their superintendents in a room and review how they communicate. Find out if the operations folks know what the discount schedules and grade requirements are for the markets we ship in to. Do we provide outside employees with the contract specs before trains are loaded?

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Review with everyone how the operations staff monitors grades during loading. Find out who oversees the grading and of they have the authority to stop loading cars. We have blending tanks – let's make sure we use them!

Make sure that all trucks are graded before they leave the elevator and that our grades are logged. And the staff has to know it isn't enough just to grade the trucks — the shipments have to be of acceptable quality to avoid discounts even if we have to unload and start over some times.

Check all the elevators to see who has any wet or damaged corn, which ones have had FM problems, and so on. It may pay us to change who loads for certain markets if we have quality problems.

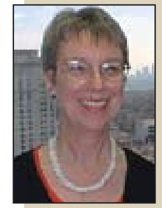
And while we're at it, let's make sure that one person at each facility is responsible for cutting down lost grain. Probably means being more diligent about sweeping around the pits or having a couple of entry-level workers to scoop up spilled grain when we're loading trains. I'm not sure what all the answers are — that's your area — but a bushel of beans on the ground costs us 12 bucks!

Let's send out a reminder to our farm customers about our discount schedules, and offer to work with them if they have quality issues in their farm bins. Perhaps we can head off some problems before they get into our bins.

I think I'll get our new assistant merchandiser involved in this. He used to be in operations himself and should be an asset for you. Maybe he can also take on some responsibilities to coordinate merchandising and operations. He understands how both sides work and folks like him.

High-priced markets can hurt a grain firm's bottom line in many ways. Discounts that are a percentage of price — or taken as shrink — and "lost" grain, are especially costly and add up quickly, resulting in eroding profits and customer confidence.

Knowing how your firm "grades out" on controlling quality and minimizing losses, can be a critically important part of your firm's operations protocol, and makes great sense in these times of high- value grains and a highly volatile marketplace. ■



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