

The Value in Grid Marketing

Story by
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If you retain ownership to feed your calves, you may be capitalizing on known genetics that provide a critical edge. You may be collecting performance and carcass data to give you an edge in selecting bulls and culling cows for greater profitability.

On the other hand, if you're selling those cattle on the average, with no regard for measurements of value beyond what the buyer's eye can judge, you have plenty of company. An estimated 75%-80% of all cattle sold are an unknown commodity until the packer discovers the true value.

What's wrong with that?

Blind commodity selling ignores consumer demand signals and adds wind to the forces eroding beef's market share of the meat dollar. On an individual level, it misses many opportunities to improve profitability — perhaps by \$30/head, researchers say.

You can gain marketing leverage by knowing complete information as to how your cattle are likely to feed and to dress. If you truly don't want to know, you will lose marketing leverage. But if you go looking for information, be ready to change.

The main tool used in value discovery of finished cattle is called "grid" marketing because it is usually represented by premiums and discounts shown in a table or grid. Premiums are highest for cattle that hit the upper left-hand corner of the grid (see Table 1). As an example of the range in prices, the U.S. Department of Agriculture (USDA) reports a weekly composite grid, "National Carcass Premiums and Discounts for Slaughter Steers and Heifers," available by mail or on the Internet at www.ams.usda.gov/mm-reports/nw_ls195.txt (see Table 2).

The average grid structure of premiums and discounts this summer shows a seasonally sharp discount for Select-grade beef and a moderate premium for all "certified program" cattle, a category that includes *Certified Angus Beef*TM product. The prices vary weekly and from plant to plant.



70-70-0

So how does anyone know where to aim? Producers often ask that question as though it has an obvious answer grounded in futility, but the overall target has not changed much in the 20-year history of the Certified Angus Beef (CAB) Program. Tim Schiefelbein, value beef procurement manager for Monfort, says, "We like to say it's a 70-70-0 target: 70% Choice or higher, 70% [Yield Grade (YG)] 1s and 2s, and zero 'out' cattle."

By "out" he means those with carcasses falling outside the normal minimum standards of Select, YG 3, 550-950 pounds (lb.) and no dark cutters. Schiefelbein says the 70-70-0 rule is actually more like a "sum 140" rule; you hit the value target if your cattle grade 90% Choice and have 50% YG 1s and 2s, or if they grade 55% Choice and have 85% YG 1s and 2s.

Over time, there are adjustments in grid-component prices to reflect the market, but that doesn't mean producers are faced with a moving target. "There is no time of the year that 70-70 is not at a premium to average cattle. Sometimes it may be worth \$30 per head over, and sometimes it may be \$10 or \$12 over, but it will always be a premium to the market," Schiefelbein promises.

Monfort's Greeley, Colo., plant last year harvested 199,421 "formula" cattle, a

term Schiefelbein uses for any cattle sold on a value-based grid. Of those cattle (all colors of hide), 8.82% were Prime, 65.38% were Choice and 13.22% were accepted as *Certified Angus Beef* carcasses. About half of the cattle were black-hided, he notes.

Yield grades slipped a little because gains in quality grade tend to come at the expense of yield. However, some cattle can do it all, and those are the ones to find, he says. One pen of cattle early this year graded 90% Choice or better and 90% YG 1s and 2s.

Schiefelbein says demand for quality has increased within the 70-70-0 target, and the grid has had to bid higher premiums to capture more of that kind of beef. But even though more than twice as much beef is sold as close-trim now compared to five years ago, premiums for lean beef have not advanced, he says. That just means those premiums are already at about the right level, he concludes. "Leanness is really important, and Angus producers sometimes forget that; but it will soon become a given in the grid target."

The need for data

Grid marketing rewards cattle that hit its targets, but the main feature for novices is the potential for penalties. Grids can be merciless when you don't

Table 1: Illustration of typical breakout of premiums (\$) and discounts (X) in a grid

	YG 1	YG 2	YG 3	YG 4	YG 5
USDA Prime	\$\$\$\$	\$\$\$\$	\$\$\$	XX	XXX
CAB®	\$\$\$\$	\$\$\$	\$\$	XX	XXX
USDA Choice	\$\$\$	\$\$	\$	XX	XXX
USDA Select	\$\$	\$	X	XXX	XXX
USDA Standard	XX	XX	XXX	XXXX	XXXX
USDA Utility	XXX	XXX	XXXX	XXXXX	XXXXX

Table 2: National carcass premiums and discounts for slaughter steers and heifers for the week of July 12, 1999

Value adjustments

Quality	Range	Simple avg.	Change from previous week	
Prime	3.00	10.00	5.17	0.00
Choice	0.00	0.00	0.00	0.00
Select	-8.00	-12.00	-10.00	+0.70
Standard	-11.00	-21.00	-18.83	+0.54
<i>Cert. programs:</i>				
Avg. Choice+	0.00	3.50	1.25	0.00
Bullock/stag	-20.00	-35.00	-25.20	0.00
Hardbone	-16.00	-30.00	-22.67	0.00
Dark cutter	-20.00	-35.00	-27.33	0.00

Cutability*

<i>Yield Grade, fat (inches)</i>				
1.0-2.0, <0.1	0.00	3.00	1.67	0.00
2.0-2.5, <0.2	-1.50	1.00	0.25	0.00
2.5-3.0, <0.4	-1.50	1.00	0.25	0.00
3.0-3.5, <0.6	0.00	-1.00	-0.17	0.00
3.5-4.0, <0.8	0.00	-1.00	-0.33	0.00
4.0-5.0, <1.2	-12.00	-20.00	-14.67	-0.17
5.0/up, >1.2	-17.00	-25.00	-19.67	-0.17

Weight, lb.

400-500	-14.00	-30.00	-20.67	0.00
500-550	-12.00	-25.00	-17.33	0.00
550-600	0.00	0.00	0.00	0.00
600-900	0.00	0.00	0.00	0.00
900-950	0.00	0.00	0.00	0.00
950-1,000	-10.00	-25.00	-17.00	+0.17
More than 1,000	-14.00	-30.00	-22.83	+0.17

Based on individual packers' quality, cutability, and weight-buying programs. Values reflect adjustments to base prices, \$/cwt., on a carcass basis.

*If yield grades are not available, yield differentials may be based on fat depth at the 12th rib using a constant of average ribeye area and muscling for carcass weight and kidney, pelvic and heart (KPH) fat. Superior or inferior muscling may adjust lean yield. Source: USDA Market News, Des Moines, Iowa; (515) 284-4460; www.ams.usda.gov/mnreports/nw_ls195.txt.

have the right kind of cattle on kill day. You need information before jumping into grid marketing, yet the grid is a major source of that information.

"It's a chicken-or-egg problem," says economist and grid-marketing expert Ted Schroeder, Kansas State University. Southwest Iowa area Extension beef specialist Darrell Busby puts it more dramatically: "Never sell on a grid without having data — that's suicidal."

Alliances, such as the Iowa-based Precision Beef Alliance (PBA), allow producers to gather data while continuing to sell on cash or "commodity grids" that have only modest premiums and discounts. Some steer futures are good educational tools, but, Schroeder cautions, many are not oriented to the "real world" of commercial cattle feeding. "At some point you just have to take a little risk, partner with a feedyard and find out what you really have," he says.

Once you gain information, experts agree long-term profitability is best served by aiming at a grid that will better reward your moves toward producing cattle of higher value.

Most grids feature huge discounts and relatively modest rewards, so you may ask, "Why take the risk, ever?" Busby and Schroeder say cash sales usually presume a standard level of "outlier" cattle, and that is figured into the bid. PBA data indicate producers can make \$15-\$20/head by managing to avoid cattle that are too heavy, too light, USDA Standard or dark cutters. Schroeder's research suggests that figure may be more than \$30/head.

Whether you are ready for grid marketing sooner or later depends on what the initial data say, Busby notes. PBA, of which Busby is an ex officio board member, routinely works with six different packer grids. "Sometimes a member will have one year's data confirm that he is roughly on target, while others wait and cull and adjust for three years before trying grid sales." Weather factors can skew any single year's results.

Table 3: Three alternative grids

	Commodity	Yield Grade	Quality Grade
Prime	\$6.00	\$3.00	\$10.00
Upper two-thirds Choice	\$1.50	\$0.00	\$3.50
Choice	\$0.00	\$0.00	\$0.00
Select	USDA spread	USDA spread x 0.85	USDA spread x 1.15
Standard	Select-\$10.00	Select-\$3.00	Select-\$15.00
YG 1	\$2.00	\$3.00	\$1.00
YG 2	\$1.00	\$2.00	\$1.00
YG 3	\$0.00	-\$1.00	\$0.00
YG 4	-\$15.00	-\$20.00	-\$12.00
YG 5	-\$20.00	-\$25.00	-\$17.00
Light & heavy carcass	-\$15.00	-\$15.00	-\$15.00

Source: Dillon Feuz, agricultural economist, University of Nebraska, Panhandle Research & Extension Center.

Table 4: Representative variation among commodity, yield-grade and quality-grade grid prices, \$, based on the following assumptions:

USDA Choice-Select spread:	\$7.00
Average dressed price:	\$100.00
% cattle grading Choice:	60
Base grid price:	\$103.80

Commodity Grid:

Quality grade	Yield Grade				
	1	2	3	4	5
Prime	111.80	110.80	109.80	94.80	89.80
Upper two-thirds Choice	107.30	106.30	105.30	88.80	83.80
Choice	105.80	104.80	103.80	88.80	83.80
Select	98.80	97.80	96.80	81.80	76.80
Standard	88.80	87.80	86.80	71.80	66.80
Out cattle	-15.00				

Yield-Grade Grid:

Quality grade	Yield Grade				
	1	2	3	4	5
Prime	109.80	108.80	105.80	86.80	81.80
Upper two-thirds Choice	106.80	105.80	102.80	83.80	78.80
Choice	106.80	105.80	102.80	83.80	78.80
Select	100.85	99.85	96.85	77.85	72.85
Standard	97.85	96.85	93.85	74.85	69.85
Out cattle	-15.00				

Quality-Grade Grid:

Quality grade	Yield Grade				
	1	2	3	4	5
Prime	114.80	114.80	113.80	101.80	96.80
Upper two-thirds Choice	108.30	108.30	107.30	91.80	86.80
Choice	104.80	104.80	103.80	91.80	86.80
Select	95.75	95.75	95.75	83.75	78.75
Standard	80.75	80.75	80.75	68.75	63.75
Out cattle	-15.00				

Source: Dillon Feuz, agricultural economist, University of Nebraska, Panhandle Research & Extension Center.

Genetics and management

Schroeder sees some urgency in moving producers toward gathering and using data to help ensure their financial viability. "The market says to get multiple observations, by cow, as soon as possible."

That says keep records connecting individual calves to cows and start building your herd's database as soon as possible because it grows in value with volume and time. But there are more immediate uses of the data you will collect on the road to value-based marketing.

"Some short-run things can make huge differences in revenue," Schroeder says. "Close management of weights at the feedlot level can mean avoiding \$15 to \$20 per hundredweight (cwt.) discounts. Closely related to that are the Yield Grade 4s and 5s, with discounts of \$20, even \$30 per hundredweight, relative to a Choice Yield Grade 3."

The "quality grade issue" has more ramifications up the line at the ranch, Schroeder notes. "You can have a major influence at the feedyard, but some cattle just don't have the genetics" to marble efficiently, he says. "Change here takes the longer-run decision-making, management and genetic selection — but it can offer big returns."

Schiefelbein says genetics and management appear to contribute equally to the end product from beef cattle, but Marcine Moldenhauer, Excel's manager of value-added procurement programs, says factors other than genetics are most important. Moldenhauer, who has a lot of experience in working with Cargill's BeefWorks and the Angus America alliance, says, "Probably 70% to 80% of the change needed is pure management, whether it be health, nutrition, sorting or pulling cattle off grass earlier."

In the feedlot, sorting to optimum finish is a must, according to value-based marketing experts. "Don't blame the cow for something we did or didn't do in the

feedyard," Schroeder says. "If you have 200 calves, even if they are fairly uniform, the ideal finish date may be in at least three different weeks."

What are the rewards? Moldenhauer says, "Some people were attracted to value-based marketing to get more for their cattle, and to get what they were worth. But after a year or two, they see it's all about learning what value is, what drives that and why — knowing how to really manage the cattle to hit the consumer target. The idea goes far beyond just putting cattle on the grid. It's a whole paradigm shift," she stresses.

Most producers just test the water in a limited way at first, she says. "With most of them, good news or bad, they say, 'I better try a little more and see what happens.' Some have a knee-jerk reaction, too: 'That's it, I'm done, I'm out.' They need to consider where they are going to fit in the future. Are they going to be commodity traders or quality producers?"

"If you have substandard cattle, ask yourself how long you can do that. You can't fool even some of the people all of the time," Moldenhauer continues. "Are you going to keep moving around? After some point are you willing to accept the reality of what those cattle are worth or make a change?"

Producers point out that discounts always outweigh the premiums. "That's true," Moldenhauer admits. But that's in the big picture — it is not true for the producer who has worked to apply the lessons learned in value-based marketing.

Choices to make

Since management affects at least half of the outcome from any cattle, you need to choose a feedlot carefully. Find a feedlot manager whose personality is compatible with yours and who can provide the services you want for your cattle. The genetics and management expertise are out there right now to achieve the 70-70-0 mix, Schiefelbein says.

Poor management can derail good genetics, but even the best management "can't ultrasound-sort garbage and get quality," he says. "Of course, the American Angus Association and the CAB Program have an advantage with the carcass EPDs (expected progeny differences).

"With other breeds, you look at that target and wonder how to get there. There are no tools other than manage-



"Each grid is a little different, some slanted toward higher grading, others slanted more toward cutability," comments **Steven Landgraf**, manager of Royal Beef, Scott City, Kan.

ment, which will get you 50% of the way there. You put them both together, and that's where the big rewards come," Schiefelbein says, noting that the CAB Program's licensed feedlots have the potential to do just that. "Get the right cattle in the right hands, and you'll really make them shine."

Once you commit to grid marketing, you still must choose your target. The value of any single carcass can vary by \$75 or more, depending on the grid market through which it is sold. There are at least a dozen established grids out there, some varying by no more than 50¢ on one item from the next grid, others seeking a very different type of carcass. With a little time and effort, you can usually find a grid that is a logical target for your cattle.

Economists refer to three basic types of grids in value-based marketing: the commodity grid, the quality-grade grid and the yield-grade grid (see tables 3 and 4). The first is considered primarily a tool for use in inventory control, but it also serves as a learning grid for a producer to decide which of the other two types of grids to target.

Most Angus-type cattle are best suited to the quality-grade grid target. Specific genetics, management and timing are critical to the success of choosing any grid target.

Steven Landgraf, manager of Royal Beef, Scott City, Kan., has dealt with at least five different grids as a cattle feeder. He also knows the other side, having served 12 years as a packer-buyer for IBP and National.

"Each grid is a little different, some slanted toward higher grading, others

slanted more toward cutability," Landgraf comments. "The secret is probably to send them to the one that favors what you have the most of." If you have cattle that can "do it all," in terms of grading at least 70% Choice with 70% YG 1s and 2s, he says, "I'd go to one with the highest premiums for Choice, CAB® and Prime."

Keep in mind that unique grids may be very similar, and the best target in the fall may not be so in the spring. "In USDA-reported grids, some of the premiums and discounts vary quite a lot over time," says Clem Ward, Oklahoma State University economist. "The Choice-Select spread, discounts for heavy cattle, [YG] 4s and 5s, and maybe 'out' cattle — the other cells in the grid don't vary much."

Read the market

After you have at least one year's worth of discovery carcass data on your cattle, perhaps from a commodity grid, you can "plug your carcass results into various grids to see which might be best," Ward says. "But recognize that a change in the Choice-Select spread might change your decision."

Landgraf agrees. "In February or September you almost hate to see a pen of Angus-type cattle grading 80% Choice when the reward is only a few dollars. It might widen to \$11 or \$12 in May or June," he says. Your cattle have to be fed until they are finished, so if your Angus-type cattle are done at a time when the rewards are seasonally lower, maybe you should try something different back at the ranch.

"Change your calving dates or your window on when they go on feed by varying your backgrounding strategies," Landgraf suggests. "People get discouraged that nobody is paying much of a premium for their good black cattle in January and February, but that's when the market wants cattle that may only grade 20% Choice but 80% YG 1s and 2s. The market changes through the year, more than some people realize."

For any grid target, dressing percentage may be the most critical component, Landgraf says. He cites one example where cattle that were fed for 37¢/lb. of gain put on those pounds at a rate of 4.25/day, graded 70% Choice and had a 30% *Certified Angus Beef* acceptance rate. But the growthy, 1,300-lb. Angus-type

steers were “heavy hided” and only dressed 62%. “The owner compared his price to a live price — which is a fictitious kind of a standard to go against — and decided that he didn’t get a premium.

“You could look at it that way,” Landgraf allows. “But you’ve got to analyze it on an animal-unit basis instead of on a live basis. The cattle still made money, but they may be telling you to manage them differently. Put them on feed a little lighter and feed them longer, so they will lose some of that middle, instead of placing them on feed as eight-weights. You have to know your cattle.”

Grid pricing is “glorified grade-and-

yield” pricing, says Landgraf, who used to buy cattle that way. “It’s like putting grade-and-yield into a jigsaw puzzle. I like that analogy; you try to have all the pieces of the puzzle that get you premiums.” Just make sure you aren’t working on the wrong puzzle or missing too many pieces to try putting the picture together.

It makes Landgraf’s job easier when a customer knows his target at placement, because management can be tailored toward meeting a specific grid. As a licensed CAB Program yard, Royal Beef is participating in building the database that will help fine-tune those abilities to increase the *Certified Angus Beef* carcass acceptance

rate of eligible cattle while optimizing profit opportunities.

There is no pen-by-pen grid negotiating, Ward says, and with good reason. “You can’t ask the buyer to blend, estimate by appearance, and adjust premiums and discounts to fit whatever kind of cattle you have. That defeats the purpose of grid marketing, which is to reward better quality and discount poorer quality cattle — not to adjust the grid to fit any cattle,” he says. “The idea is to change cattle so that they fit a grid.”

