

DIRECT MARKETING BEEF: PROS AND CONS, DO'S AND DON'TS

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INTRODUCTION

Many ranchers are trying to direct market beef, including ranchers in western Colorado. Our experience with these ranchers and others is outlined in this presentation. There are many valid reasons to use direct marketing. One specifically is to supplement ranch income. Of course, there are also reasons not to direct market beef. Examples include: increased liability, low economic returns initially, and very time consuming.

Four main items should be addressed before you begin a direct marketing beef program:

- 1) You must have a niche that will differentiate your beef products.
- 2) Prepare a well-written business plan that actually forecasts a profit.
- 3) Form a business entity (separate from the ranch) in order to minimize liability.
- 4) Know the capabilities and limitations of your products' processing, packaging and distribution.

THE **PROS** OF DIRECT MARKETING BEEF

Direct marketing is not about joining an existing alliance or established program like Certified Angus Beef or US Premium Beef . It is about the niche you and possibly your neighbors think you can create in the market. Today, everyone is trying niche marketing. As a result, your niche must be **NEW** and **DIFFERENT**, as well as **VALUABLE**. Examples include: Conservation Beef , Yampa Valley Beef, Homestead Beef, Oregon Country Beef , Rocky Mountain Beef TM etc.

The following three reasons are why direct marketing beef should be considered:

- **Increasing your income.** Cattle ranching is a commodity based business in which there are only three ways to make more money. The first is to raise more beef, which is increase cow numbers and/or pounds weaned. The second is to capture more value per unit by retaining ownership. Lastly, add an enterprise on the ranch that captures money from an existing resource base not presently generating income (like game hunting). Adding a direct marketing beef enterprise can potentially increase income by retaining ownership and adding a new enterprise.

- **Creating a positive image for the beef industry.** You can establish a new identity that attracts positive responses from the general press or a specific group. Your motivation to direct market beef may be based primarily on the positive image you create for the beef or ranching industry.
- **Increasing demand for beef.** The enterprise must still be at a break-even return, however, it *is* possible to increase beef consumption also. I see opportunities targeted at people of Middle Eastern cultures. If Argentina can import grass fat beef and sell it for a premium, why isn't someone in the Sand Hill of Nebraska doing the same thing? Why aren't you selling a quarter of beef to hunters on your ranch? (There are ways to increase beef demand and YOU might be the person to do it!)

THE CONS OF DIRECT MARKETING BEEF

There is always reason for caution when looking at starting up your own business venture. Before that first load of cattle is taken to the packinghouse, consider these points:

- **Most small direct marketing attempts don't make a large profit in relation to the effort that it takes to get them started.** There are hundreds of steps and considerations that must be taken prior to ever selling a single animal or cut of meat. You might be way ahead financially by seeking off-farm employment rather taking the time and effort to direct market beef.
- **By direct marketing beef, you might simply be substituting labor for the ranch, versus labor for direct marketing beef.** Be sure you are *adding* value, not substituting it. Is the ranch business suffering because of the effort to direct market beef?
- **You have verifiable trace back when choosing to direct market beef.** There is an increased liability when direct marketing a food product. Depending on your business structure and insurance, you may be risking the whole ranch just for the opportunity to sell a few head. Be totally aware of the liability to you and your ranch before you ever direct market beef. An inferior product or one that's proven to be a health concern might be the processors fault, but it *is* your label.

THE DO' S AND DON'TS OF DIRECT MARKETING BEEF.

Create an Identity

You need to find some type of niche or marketing gimmick that sets your product apart from any others presently in the market. The reality is this: Beef is generally a generic product within a certain quality grade. You must convince the consumer that your beef is somehow different. This distinction can be anything that you can substantiate and the consumer can buy into. Making false claims or claims you cannot back up is a definite "Don't" for direct marketing beef.

There are many valid claims you can make to differentiate your product. Examples currently used include: ranch or livestock management claims like conservation, free roaming, natural or organic; quality claims such as dry-aged, corn-fed, or grass-fed or locality claims such as Oregon Country Beef or Yampa Valley Beef. Market research shows consumers will pay a premium for knowing their food source. What is the niche that will set your direct marketing project above the rest? This is a must DO for success. No matter what your claim, have a record keeping system that can substantiate it. Labels need approval by USDA Labeling Review department. The more claims you make, the more documentation you will need to substantiate them. It is generally recommended to hire the services of a company that specializes in obtaining label approval. Label approval can take as long as six months and many mistakes can be avoided by following the recommendations of the consultants. Remember, that most consumers read very little detail on a label, so keep the message simple.

Direct marketing doesn't have to be a year-around project. If you study gift buying, you'll find that approximately 75 percent of all food gifts are sold for the holidays. Seasonal marketing, given a ranch usually has a seasonal delivery of live cattle, makes solid sense when considering direct marketing. Other food products are seasonally marketed successfully. For example, Olathe Sweet Corn has become a sought after seasonal product worth its premium price.

Direct marketing beef is not about being the best commodity marketer. As sellers of live animals, we are not accustomed to being retail or wholesale marketers. Generate some marketing ideas by familiarizing yourself with retail marketing strategies. Don't think like a commodity marketer! To illustrate, women buy most of the food for households in the United States. There are entire books and courses regarding marketing to women. Have you read them? Were you going to sell beef directly and not know the primary buyer? Your job now is not to sell the carcass, but "Sell the Sizzle" from the carcass.

Do not overlook the idea that your sizzle is more than beef. A great marketing logo can go on more than a package of steak! Piggyback the beef product into ancillary goods, such as t-shirts, hats, cups, etc., which may ultimately have a higher markup value.

Try to profile your customer from the beginning. Find out their needs and lifestyle. Do some demographic research. It often makes sense to have a potential customer advisor (or personal business coach) for your business who can make you aware of paths to successes and possible challenges. Your customers who buy into your creative ideas and believe in your products will want you to succeed, too!

BUSINESS PLANNING

Do not just create a great idea in your mind and go forward. Take the time and effort to write a complete, comprehensive business plan. The process of committing an idea to paper is invaluable. Use the many resource materials available on how to write and use a business plan. Include financial projections, marketing strategy, processing system and product distribution. Following a business plan verbatim may be impossible, but once the groundwork

is laid you will have the wherewithal to pick and choose the actual process steps. To succeed you must have commitment to the program, diligence to remain on track and a lot of perseverance! Of course, many unforeseen challenges and opportunities will present themselves. The plan is a guide, a work in progress. The plan must be able to show you a profit! If you cannot plan on a profit, then there is little reason to try direct marketing. Many direct market food businesses take five to eight years to realize a steady profit.

Part of the business plan must include carcass yield information. You need to know, on average, how many pounds of product each animal will yield and have that broken down into yield per cut type. It is not unusual to lose 25 to 30 percent of the hanging weight in the cutting process. This would mean that if a side of beef weighed 300 pounds, there would be only 210 to 225 pounds of trimmed retail cuts. By knowing this information you can calculate breakeven prices for beef products at the retail or wholesale. In processing, there is a considerable amount of loss due to the amount of external fat, cutting loss and shrink from dry aging. Dry aging increases the standard shrink by 3 to 4 percent. The longer carcasses age the more they shrink. Calculate shrink into your breakeven point.

Your plan must also address how you intend to sell the whole carcass once it is turned into cuts and packages. It's easy to sell the high-value cuts (like the loin) but these are a small percentage of the whole carcass. What are you going to do with the whole front half? A typical 700 pound carcass will have 150-200 pounds of hamburger. Profit will be tied up in inventory unless you have a viable sales outlet for the lesser value cuts.

BUSINESS STRUCTURE

What sort of business structure are you going to use to direct market beef? It is a critical decision for liability, investment opportunity, taxes, etc. Seek legal advice on the best business structure available for your particular business plan. There are many business forms you can choose when setting up your direct marketing enterprise. Business structures used by other direct food marketers include: traditional cooperatives, marketing cooperatives, and now a new cooperative called "third generation cooperatives". Limited Liability Companies (LLC) or Limited Liability Partnerships (LLP) are also used by other direct marketers of beef. Traditional business structures include Sole Proprietorship, Subchapter S Corporations and C Corporations. You need to understand all of the ramifications of whichever business structure you chose. A common business practice is separating the ranching entity from the direct market beef business. Once you have decided a structure and if it involves more than one family, make the degree of ownership high enough that partners or members will commit sufficient time and capital. Making ownership a nominal fee brings nominal commitment to the effort. A non-profit structure is plausible if your motive is not solely to increase income.

PROCESSING AND PROCESSORS

By their nature, direct beef marketing will require you to have relationship with a small or medium sized processor. With few exceptions the processor must be USDA inspected. A good custom processor is not the same thing as a good commercial processor. Custom

processors have procedures that need to be examined in order to ensure consistency of beef products. Items that need to be assessed with the processor include: hamburger lean-to-fat ratios, the consistency of the processing, how fast the beef can be frozen, proper storage space to allow carcasses to hang 14 or 21 days, inventory space, bar coding and packaging technology, and distribution of products. Involving a meat scientist with processing is imperative when considering product quality. The ultimate goal of any packaged beef product is to have consistent quality over time. The processor should be in close proximity, ensuring feasible transportation costs of trucking livestock to the processor and beef products to a retailer.

Do not assume managing your inventory is the processor's responsibility. They may be able to store product for you, but do not presume it is their priority to manage it.

FINAL CONSIDERATIONS FOR DIRECT MARKETING BEEF

Relying on volunteer labor to get the project off the ground is fine ~ up to a point. You need to plan for the cost of labor over the long term. Your labor is not free and your business plan must include these costs.

One of the **biggest challenges** in direct marketing beef, when you have a group of ranchers involved, is managing the relationships, making group decisions, and delegating responsibilities. The greatest idea and most sound business plan can fail from lack of effective communication methods. When making decisions as a committee member, remember to keep the discussion on the issue and not the person. You also need to have a decision maker appointed. There will be circumstances when a decision has to be made that cannot be decided by committee. Someone must have the authority to make a decision, which is backed by the rest (right or wrong in hindsight). The bigger the group or executive committee, the more challenging the communication and decision-making becomes. Managing the communication is one of the biggest challenges a direct marketing effort will face.

A big DON'T is using livestock terminology to describe your beef product. Food editors or reporters don't know your terms and they may not be appropriate anyway. You don't say "We take cull cows and turn them into hamburger." They might ask what a cull cow is, and you really don't want to explain that term! Check out marketing and promotional quips for similar products on TV, in magazines, and on the Internet.

As commodity sellers, you are accustomed to being paid for your livestock promptly - it's the law. As a direct marketer, you will use an Accounts Receivable System. It is often overlooked that there's a longer time lag between delivery and payment for product in wholesale and retail. You must be prepared for this time lag and realize a certain percentage of your cash profit will always be tied up in account receivables and inventory. This time lag can be a real challenge for start-ups that are operating on very little capital.

Do not try to compete with established wholesalers or processors on price alone. You cannot begin to process beef more cost effectively, have a streamlined delivery system, or the capital

to run an advertising campaign that established beef processor/marketer does. It would be like building a superior pickup in your shop and trying to compete with Dodge, Chevy and Ford. You might build it better, but you cannot compete for very long on price.

The meat processing business is very competitive. Established processors, wholesalers and distributors will not just let you take market share. Be prepared to do business with your competition!

Now is one of the best times to start your own direct market enterprises. These efforts are part of USDA's rural economic development goals. They support them with low interest loans and even grants. These programs can assist you with needed start up capital at little or no cost.

Start small, so your mistakes don't cost you the entire endeavor. Be able to afford your errors.

FURTHER REFERENCES

Colorado State University's Animal Science and Agriculture Economics departments along with American Farmland Trust recently created a web site specifically for niche marketing of beef. The site goes into greater detail on niches, business plans, existing examples and links to more information. The address is <http://dare.agsci.colostate.edu/aftnichebeef/>

CASE STUDIES



Background

Yampa Valley Beef was an idea developed out of several discussions among ranchers, Conservancy members, and the local Economic Development Committee (EDC). The concept of selling a beef product that tasted great and protected the working landscapes come from the Nature Conservancy and their desire to test market the concept. In the fall of 1997, they proposed a small market test of this idea. At the same time, the local Economic Development Committee expanded its membership and formed an agricultural subcommittee. The EDC was looking for a project that could tie the area's ranches and the resort economy closer together

and seek ways for agriculture to profit from a resort economy. They chose a beef project, seeing that it was the largest segment of the local agricultural economy.

These community members combined and began the concept of Yampa Valley Beef. In 1998, the group met and determined product processing, marketing strategy, and conservation components. Throughout the year the project gained the financial and in-kind support from the Colorado Department of Agriculture, Colorado State University, Routt County, Cooperative Extension in Routt County, City of Steamboat Springs, Routt County Cattlemen's and Women's Association, the Nature Conservancy, and the Steamboat Springs Chamber and Resort Association.

The Mission of Yampa Valley Beef is "To develop an expanded market for locally produced brand name beef as a tool for improving the economic viability of ranching in the Yampa Valley while preserving agricultural lands and the natural communities they support." To accomplish this mission, the company pays a premium for cattle to member ranchers and also requires that at least 25 percent of the cattle must have been grazed on lands protected from development with a conservation easement. Lastly, a portion of the annual profits will be given to a land conservation organization.

In December 1998, the company began selling their first beef products. Hamburger patties were made available and sold to area restaurants and retailers, and premium beef bundles were made directly available to consumers. The first customer of Yampa Valley Beef was Hazies restaurant at the Steamboat Ski Area.

In March 2000, twenty-two ranchers and business people had ownership in Yampa Valley Beef, LLC. Yampa Valley Beef's member ranches managed over 42,000 deeded acres, 15,000 leased acres, and over 5,000 acres of land under conservation easement. The average member has ranched in the valley for 31 years. Yampa Valley Beef marketed its products to 15 area restaurants, guest ranches, and retail outlets. Hamburger patties were the primary product of the company; and premium beef bundles were offered again for the 1999 Christmas season. Over 25,000 pounds of beef products were sold in the 1999 - 2000 ski season.

In 2001, the membership of Yampa Valley Beef voted to change the entity from a Limited Liability Corporation to a Non-profit Corporation, to better address insurance issues. Yampa Valley Beef decided to temporarily close the doors and work on the business organization and work on product quality and consistency.

In the fall of 2003, a team of college graduates who had a vested interest in Yampa Valley agriculture re-evaluated how committed the community and the consumer was to the initial effort for success. The team put together a business plan, company goals and strategies, then proposed those ideas to the Yampa Valley Beef members. The members agreed to let the team move forward with Yampa Valley Beef, and in August 2003, beef products were available to consumers. Yampa Valley Beef still offers hamburger patties, and has added all beef frankfurters, and summer sausage, along with Yampa Valley Beef ball caps and branded leather coasters.

COLORADO HOMESTEAD RANCHES

Colorado Homestead Ranches (CHR) is a cooperative of ranches that have organized to raise, process, and sell their free-range beef at various local sites throughout the Western foot of the Colorado Rockies. CHR currently sells primal beef cuts to over 750 local customers, several area restaurants, at weekly farmer's markets in the resort communities of Aspen and Glenwood Springs, and most recently, from their retail storefront in Paonia, Colorado, Homestead Market. Over the past five years, the business has sustained a 20% growth rate.

CHR began in 1996 with a harvest of 16 animals and has steadily increased that number to 84 in 1997, 88 in 1998, 94 in 1999, 103 in 2000, 140 in 2001 and 180 in 2002. Consistent, manageable growth is the result of determination and a managerial commitment on the part of each producer, cooperation among the producers and clearly defined production objectives. CHR's primary mission is to increase the share of its producers' cattle herds that are processed and marketed through CHR activities.

CHR has established itself as a premier beef producer and marketer, as well as a loyal, community citizen and steward. CHR takes pride in the fact that all cattle are born and raised on family-owned operations, then fed on the open range until they are finished in a small, non-commercial feedlot maintained on one of the five ranches. With such care invested in raising quality stock, limiting exposure to stress and reducing susceptibility to disease, CHR is able to eliminate the use of all feedlot antibiotics and hormones in order to provide an all-natural product, something of utmost importance to the consumer.

Full carcass utilization to improve profitability is the most recent emphasis of CHR marketing activities. Primal cuts were traditionally priced higher and had a higher profit margin than the chuck and ground beef portions of the carcass. While the chuck and ground beef portions of the carcass were priced lower than the primal cuts, they were not selling as quickly. A few years ago CHR began a business venture of producing processed meats (bratwurst, polish sausage, meat sticks, jerky, and summer sausage) from the lower valued beef cuts. In the first year of processed meat sales, the company's income increased by \$11,000. The success of these products inspired the producers to expand their product lines to include more value-added products. More recently, Colorado Homestead Ranches chose to explore the market for ready-to-eat beef entrees. CHR's direct marketing efforts and innovative value added products have increased the success and profitability of the company as a whole.

The group's venture into slightly processed meats (bratwurst, polish sausage, meat sticks, jerky and summer sausage) and ready-to-eat entrees fueled interest in developing a more stable, direct marketing venue. Thus, CHR opened up Homestead Market in Paonia, Colorado in May 2002 for daily sales of all CHR product lines, in addition to meat, dairy, fruit, vegetable and lightly processed products from other Colorado value-added producers. These product and marketing developments have increased the company's sales. So far in

2002, sales have increased 35% over the same month last year and the retail market is still in the early stages of establishing a customer base. CHR's goal for 2003 is to use 200 of the producers' cattle, continue to offer managerial and marketing labor as an indirect financial commitment (with grant support for working capital) and continue to pay approximately \$1400 per head back to the independent ranches.

Other previous research in the natural beef market reveals interesting findings. Consumers are willing to pay a higher percentage premium for natural ground beef than for natural beefsteak. At a premium of 36%, the market share of natural ground beef was estimated to be 25%. (Sparling, Thilmany and Grannis, 2001).

Based on the research discussed previously, a portion of the survey was designed to gain knowledge on the type of information consumers looked for when purchasing beef products. The survey asked consumers what specific product attributes they looked for when purchasing beef products. This information can be used to determine optimal labeling and promotional strategies, and may provide CHR insight on potentially profitable production methods, such as natural or organic production (from a niche marketing standpoint).

In this survey, consumers rated *fresh* as the most important attribute; the average rating for fresh was a 4.67. *Fresh* was followed by *high quality* with a rating of 4.62. The lowest rated attributes are *pre-seasoned* (2.24), *ready to heat* (2.55), and *family pack* (2.66). When considering words that appeal to consumers and labeling, *Natural* (4.08) rated above *Grass-fed* (3.71) and *Organic* (3.37). An interesting note is that when comparing organic and natural, the word "Natural" ranked higher as being an attribute the consumers look for when purchasing beef products even though its production implications are less substantial. *Nutritional Value*, *Locally Grown*, and *Source Assurance* proved to be relatively important with a rating of 4.49, 4.22, and 4.23, respectively. See Figure 2 for more details. Although broad wording makes it difficult to interpret what consumers perceive about products using these words on labels, all are attributes that Colorado Homestead Ranches could utilize to entice consumers to purchase their products

Motivators to Purchase Locally

Studies conducted in the early 1990's focused on consumers' preferences for products produced "regionally" or "locally." These studies indicated a potential premium or niche market for specific types of "locally grown" products. As a result, a growing number of livestock producers have begun to explore this niche as a potential alternative to the traditionally low margins received in the commodity beef industry. A potential marketing alternative for CHR is a "local" or "regional" branding strategy. In order to understand the general motives that encourage consumers to choose local over non-local products, the survey instrument in this study asked consumers to rate (on a scale of 1-5 (5 being the highest)), the different reasons that encourage them to purchase local products.

Literature cited: Rosenstiel, K. et al., Feasibility Study, 2002.

