

# CATTLE BUYERS WEEKLY

MARKETING AND BUSINESS NEWS FOR THE BEEF INDUSTRY

## Program Helps Reduce Price Volatility

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PRICE volatility makes it difficult for packers to match production and prices with demand and make money at the same time. But one major packer is using a highly sophisticated computer program to help it do that. The results appear to be promising. Cargill Meat Solutions (CMS), the nation's second largest beef processor, is using a program that it says has reduced pricing volatility and improved its margin structure. It has been using the SignalDemand system for two years. Cargill's beef business has definitely performed better during that time as a result of using the system, says Herb Meischen, CMS's vp of strategy and business development.

SignalDemand, based in San Francisco, Calif., developed its "Price and Response" software system after CEO Mike Neal began the company in 2004. Earlier in 1999, he started another company to help retailers set prices. This led him to want to continue upstream to set wholesale prices as well, and apply a form of retail category management at the manufacturing level, he says. The system's goal is to optimize demand in a commodity business by helping manufacturers measure price sensitivity product by product, channel by channel, he says. The system's software includes thousands of variables and contains hundreds of millions of permutations. On the live animal side, the system plugs in live cattle futures prices, USDA weekly live cattle cash prices and CMS transactional data. On the processing side, it plugs in processing costs and planned production hours at each of CMS's plant. The planned hours is a key input, says Neal. The system also plugs in other transactional data, including packer push lists of items and current and committed supply data. The system has models for each of the markets in which CMS sells its products: spot, mid- and long-term. The system runs multiple times per day for the spot market and on an as-needed basis for the other two markets.

### System Helps Avoid Fire Sales

The system's single biggest value is that it has reduced price volatility, says Meischen. For example, if there is only 4% price volatility from the lows to the highs in the entire beef cutout each day, price levels are much easier to sustain. Neal agrees. A packer might set a high price on an item on Monday but be forced to have a fire sale on Friday. The system

recommends a more reasonable price to start the week. A big value of the system is to sense price anomalies early and make adjustments, he says. The system's second main value is its aid to decision-making, says Meischen. Due to its sophistication, the system enables CMS to synthesize many more inputs than it could historically. The weighting of each input is very different to before, he says. The system benefits both CMS and its customers because it enables one to keep a value in the marketplace longer. The system also helps CMS on the cattle procurement side, he says. So it helps plant scheduling. There's a ripple right back through the business. As a result, CMS has run its plants more consistently at a certain level over the past two years than previously. CMS now uses "score carding" to know when it is in a range of optimum value pricing, he says. Phase 2 is to align this with operations, by score-carding actual plant operations. This will determine what hours each plant will operate at each week, he says.

The system has enhanced CMS's ability to forward contract, says Meischen. As noted, the system reflects the spot market (0-21 days), the mid-term market (21-56 days) and the long-term market. The system was tuned in this way because retailers plan their beef ad activity 5 to 8 weeks out, he says. The system helps CMS to quote customized pricing for every cut, with confidence that each price is value-based and fair, says Neal. It increases its profit in the spot market by managing optimal percent sold for each cut and price in each forward time period. CMS can also run what-if scenarios to see if the impact of changes in costs and other variables. It can drive retail ad-feature activities more proactively through price and product recommendations. The system also reports on price variances and recommends corrective action. CMS also works with foodservice customers to develop menu pricing, he says. CMS has just started using the system in its pork business as well. Hormel Foods Corporation is using the system and several other meat companies are interested in it, says Neal. SignalDemand offers the system on a term license, with a subscription fee based on business volume.