

The Real Importance of Conversion

THE RECENT bull market in beans and products has caused a good deal of conjecture as to the potential impact of this price move on the earnings of soybean processors individually and as an industry. Group earnings will probably be helped moderately as the industry at any given time is likely to be only partly hedged. In a market such as we have had, many crushers would be more lightly hedged than usual. Although they are actually in business to make money crushing and not speculating on inventories, it is very difficult to resist having an opinion. This, in turn, results in tailoring hedging to their market views.

For instance, when offering firm on a 24-hr. oil export tender, the question that always arises is whether to lift hedges before the tender, lift half of them if he thinks that his chances are fifty-fifty, or lift none of them and wait for the tender replies. In practice, what often happens is that the crusher does the first when he is bullish, the second when he has no feeling, and the third when he is bearish.

Now each one of these is, or can be, a legitimate approach to this particular protection problem and might be practiced at any time by any company. However in a bull market such as this, there appears to be a marked tendency to practice the first almost exclusively, the second occasionally, and the third seldom. As long as the market keeps going up, this semi-speculation is an aid to total industry earnings as the successful sellers are working on a good basis and the unsuccessful sellers may well have paid no cost for their market protection and might even have made a scalping profit. However unless a pretty

wide-open operation is undertaken, the more important determinant of profitability is not inventory trading but the conversion level. (See "How Cheap is Cheap?" J. Am. Oil Chemists' Soc., December 1960.)

TO THOSE not forced to live with this relationship it assumes the form of an academic problem, an interesting phenomenon that exercises a devious control over the chalk marks. To the crush-plant executive however, the relationship of beans to oil plus meal is quite real and is as close as a wolf at the door. Low crush profits can mean a painful cut in total company net. This has a bearing on dividends, price earnings ratio, the price of the stock, and consequently on the ability of the firm to tap the money market. So the ramifications can be far-reaching.

Of course, the pain of the earnings cut will be more or less severe to the extent that the firm's other divisions produce income. Some firms are more diversified than others. A few are so completely diversified that jiggles in conversion have no visible effect on earnings. Less-diversified firms show varying degrees of response (Figure 1). This figure must be used with some care as the conversion levels are Illinois averages unweighted by volume whereas company profits are obviously per bushel times volume at all sorts of locations.

High-level profits on low volume can mean less money in the cash register than high volume at moderate profitability. Even when volume is known or can be estimated, another guess must be made before attempting to forecast individual firm earnings from conversion change. One

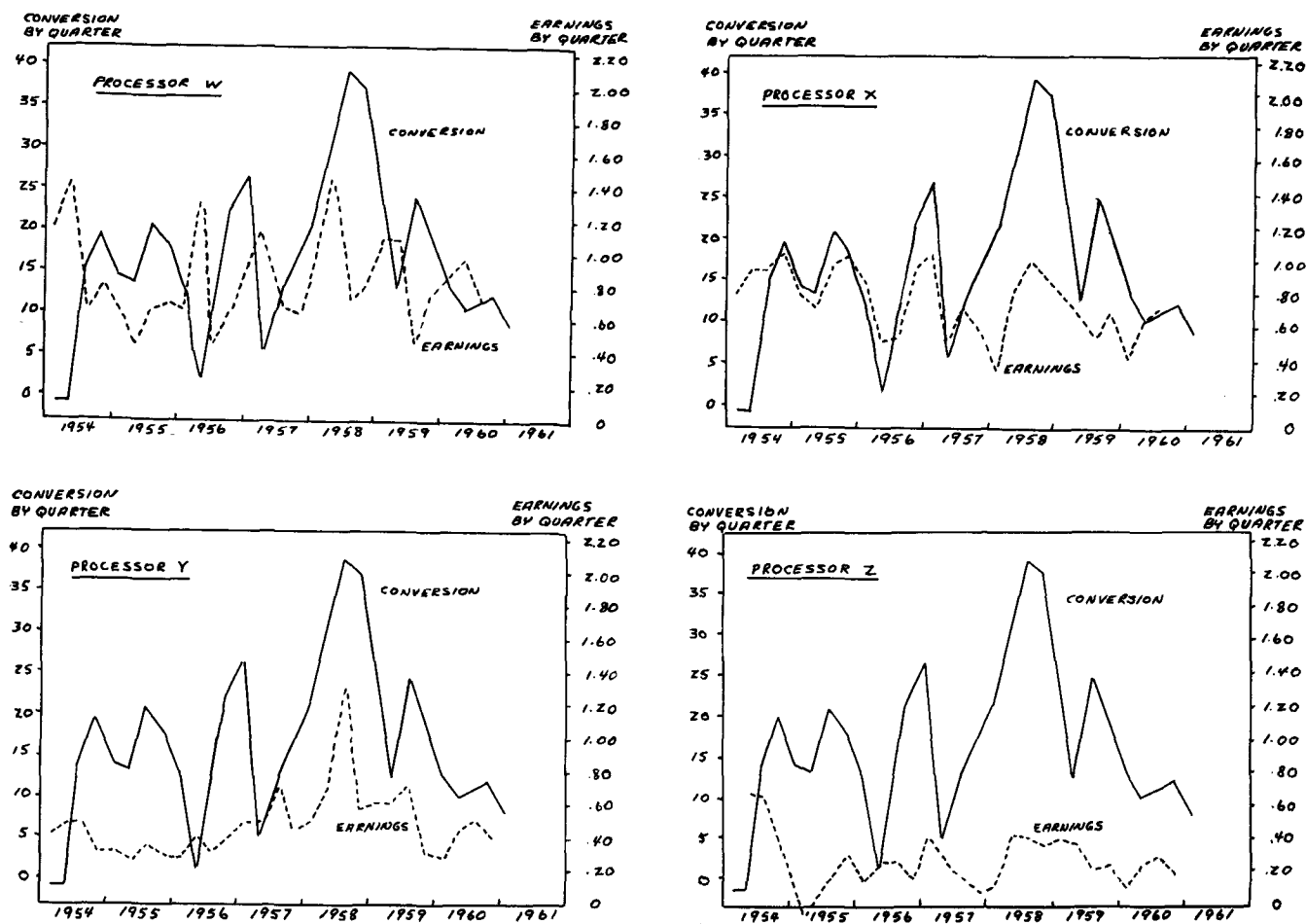


FIG. 1. Illinois crush profitability as computed by U.S.D.A. vs. quarterly earnings of selected crushers, 1954-1961.

must decide whether the type of diversification in the case of that individual firm is of a stable income nature, cyclical with bean-crush profits, or potentially contra-cyclical. If the latter, then each outside division would have to be weighed on its own merits. For instance, contra-cyclicity might appear in certain years in either the mixed feed business or in oil refining or both. Either raw product or both might be helped up by big overseas demand. This might mean big crush profits.

However the high oil prices might put pressure on refining margins and/or on the margin between crude oil and retail prices if final products are sold. High meal prices might hurt domestic consumption as well as mixed feed margins. On the other hand, apparent low profitability might be offset by good domestic meal and oil business at good profits.

So the total picture must be considered. So far this year we have seen very large crush volumes at only very modest profitability. At times like this it is most difficult to guess anybody's earnings as the other divisions may be quite important. Also very important will be how well the firm traded the market during the period. In the final analysis it is what shows up on the income statement that counts, but don't underestimate the real importance of conversion.

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• Hobby Department

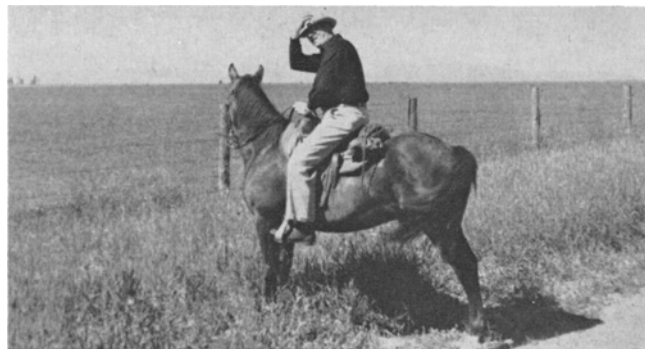
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Then Mr. Konen discusses the merits of fishing for trout and bass. "We prefer trout fishing," he comments, "but in Minnesota and Wisconsin the season is only four months long, and good trout spots are few and far between. So we make as many trout trips as we can and fill in with bass fishing. When the bass won't bite, we fish for anything that swims."

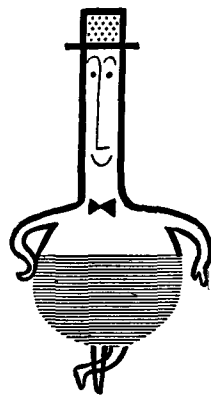
Switching from the Midwest to Montana, Mr. Konen reports that "the high spot of our Waltonite experiences is two trips to Montana, where we packed into the mountains for trout fishing. Each of these trips was of a week's duration, and the weather was perfect, the scenery beautiful, and the fishing fabulous. The only sore point was the miles of travel on horseback. Since both of us are fairly enthusiastic amateur photographers, the mountain fishing trips provided us with an opportunity to take many beautiful 35-mm. color shots. One we shall never forget is the picture of a mountainside so densely covered with bear grass in bloom that it looked as if covered with snow."

On the subject of flies, he indicates that their "favorite bass flies are the Yellow Sally, the Gray Ghost streamers, the Mouse, and cork-bodied poppers. For trout we most often use the Mosquito, the Black Gnat, Brown Bivisible, and the Neversink dry flies. Wet flies we find best are the Woolly Worm, the Black Hoof, the Black Gnat, Blue Dum, a gray hackle streamer, and Ronyak's "Secret Weapon."

Finally Mr. Konen mentions winter activities. "Walt does a bit of fishing through the ice, but I am not an advocate. However we both tie a few flies, read about fishing, and talk fishing. This is where Walt shines; you should hear his story about the trout that baited his hook or his



W.O. Lundberg



Meetings

A.O.C.S. National Meetings

- 1961—St. Louis, Sheraton-Jefferson hotel, May 1-3
Chicago, Pick-Congress hotel, October 30-31, November 1
1962—New Orleans, Roosevelt hotel, May 7-9
Toronto, Royal York hotel, October 2-4
1963—Atlanta, Atlanta Biltmore Hotel, April 22-24
Minneapolis, Radisson hotel, September 30-October 2

A.O.C.S. Section Meetings

- North Central—bi-monthly at the Builders' club, Chicago, 6:30 p.m.
Northeast—first Tuesday of February, April, and June, at Whyte's Restaurant, New York, 6 p.m.
Northern California—May, September, and November at selected places
Southwest—second Thursday of every other month, beginning January, at Rodger Young Auditorium, Los Angeles, 6:30 p.m.

Other Organizations

- March 27-31—4th Symposium on Temperature, sponsored by Instrument Society of America, Veteran's Memorial hall and Deshler-Hilton hotel, Columbus, O.
April 4-6—3rd Annual Gas Chromatography Institute, Canisius College, Buffalo, N.Y.
April 9-13—American Industrial Hygiene Conference, Sheraton-Cadillac hotel, Detroit, Mich.
April 10-12—30th Annual Meeting of the Inter-Society Color Council, Sheraton hotel, Rochester, N.Y.
April 12-14—26th Annual Chemurgic Conference, Sheraton-Gibson hotel, Cincinnati, O.
May 16-18—Maxwell Colour Centenary, Royal Institution and Imperial College, London, England
May 22-Sept. 18—Nine sessions of Ansul Chemical Company's 1961 Fire School, Marinette, Wis.
June 19-23—Air Cleaning Institute, Harvard University School of Public Health, Boston, Mass.
July 27-Aug. 1—International Symposium on Macromolecular Chemistry, Montreal, Canada
August 2-5—44th Canadian Chemical Conference and Exhibition of the Chemical Institute of Canada, Queen Elizabeth hotel, Montreal, Canada
August 6-12—18th International Congress of Pure and Applied Chemistry, Montreal, Canada

'Ave Piscatores' joke. All I can reply with is the story of my trophy-sized trout that ended in the frying pan by mistake."

Both Dr. Lundberg and Mr. Konen have been active in the American Oil Chemists' Society. The former was elected to the Governing Board as a member-at-large in 1960 and has served on such committees as Bond Award, Fat Analysis, Education, and Journal. The latter was president of the Society in 1958 and has been on such committees as Education, Membership, Fat Analysis, Smalley, Seed and Meal Analysis, Nominating and Election. He was a member of the San Francisco program committee in 1950 and chairman of the Minneapolis convention committee in 1954.