



# Ottenberg's Bakery Fermenting Ideas

Winter 2013



Four times a year, Ottenberg's Bakery publishes *Fermenting Ideas*. Our objective is to deliver an in-depth look at a single issue confronting the food service industry. There are no easy answers. Facts help each of us craft individualized solutions.

Consumers decide each day on where they will eat their next meal. Long-term success in our industry requires responding to important food trends. Ottenberg's Bakery has products designed to help. We encourage you to contact us and learn more about Ottenberg's Bakery and our products.



## A Word from Ray Ottenberg

This edition of *Fermenting Ideas* focuses on providing our readers with a deeper understanding of the forces that impact the cost of a loaf of bread. We hope that knowledge translates into increased ability on your part to plan and take actions to make your business more successful.

We are not going to cover all the important costs that affect the price of a loaf of bread. Subjects like health care and cost of regulation are far outside our limited area of competence and will be ignored for this discussion. You do not need us to explain the impact of these kinds of costs.

Ottenberg's Bakery has experience helping our customers succeed in times of inflationary food costs. We cannot suspend basic laws of economics. The price we charge has to cover our expenses. We have found that a supplier, distributor and operator working together can find ways to avoid some costs and contain/reduce prices.

Success requires a collaborative effort and some creativity. The results can be significant.

Please contact us if you would like to talk about ways to better meet any of your bakery needs. (Contact information is on back page.) As always, we would love your feedback on any of the information in this edition of *Fermenting Ideas*. It helps us correct our multitude of mistakes.



## It is One Big Market

Wheat, corn, soy beans and rice are the big four grains that form the foundation of the human diet. Animal proteins, including fish, are increasingly raised on grain before being brought to market. Beef, pork, poultry and fish production is really "further processing" of grain crops.

There are discrete markets for each grain and national markets in each of the major producing countries. But all the markets are interrelated. A drought in Australia impacts the price of wheat in the USA. High prices for corn makes wheat and soy beans more expensive.

The reasons are straightforward.

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## It is all One Big Market

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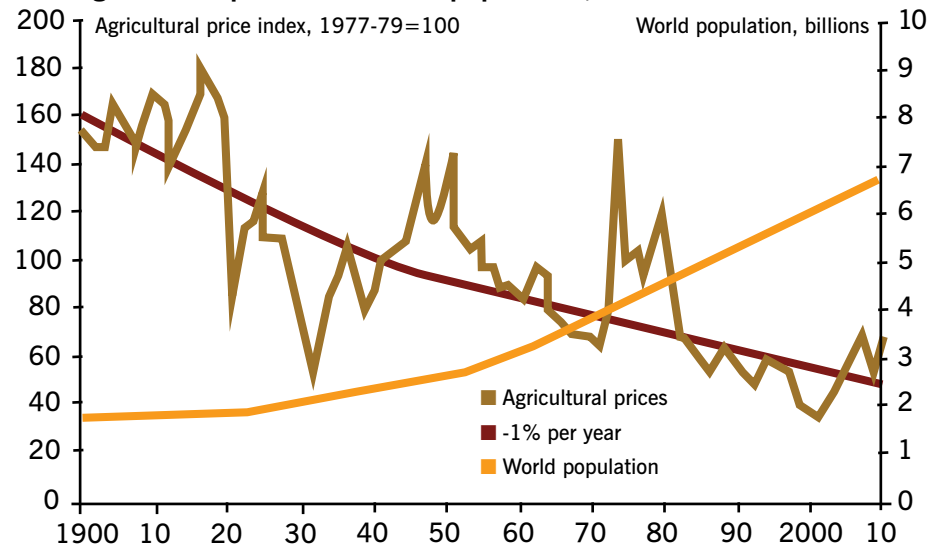
First, the grain market is international. USA wheat is shipped all over the world. When a developing country buys wheat to improve the diet of its citizens, demand increases.

Second, it is relatively easy for some users to substitute one grain for another. For example, a feed yard normally finds corn the most cost effective grain for their purposes. If corn costs shoot up, they can switch to wheat. The result is that demand for corn increases the cost of wheat.

For wheat, there are four big exporting regions (North America, Argentina, Australia and Russia) and a problem in one region will impact the overall market. A problem can be any of a wide range of issues - everything from weather to politics to currency exchange rates.

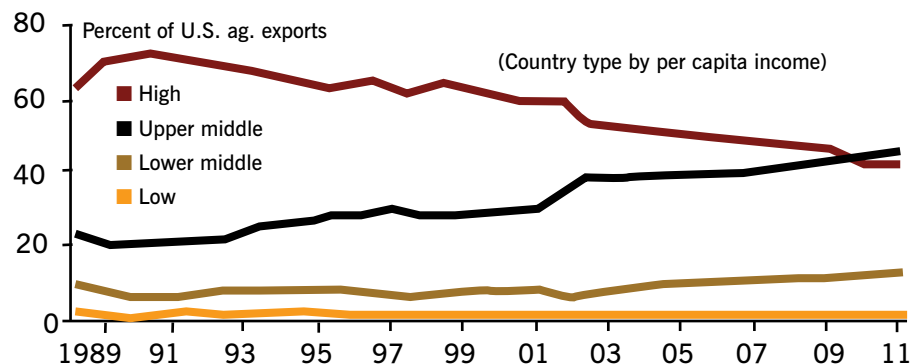
Another long term dynamic is the rising standard of living in developing countries. As citizens in countries like China and India grow more affluent, their diet changes. Overall consumption of calories goes up and meat consumption increases. Since it requires approximately six pounds of feed to produce one pound of beef, demand for meat increases demand for grains.

## Real agricultural prices and world population, 1900-2010



Source: USDA, Economic Research Service. Depicted in the chart is the Grilli-Yang agricultural price index adjusted for inflation by the U.S. Gross Domestic Product implicit price index. The Grilli-Yang price index is a composite of 18 crop and livestock prices, each weighed by its share of global agricultural trade. World population estimates are from the United Nations.

## Share of U.S. agricultural exports by income group, 1989-2011



Note: Income groups are based on per capita gross national income (high income = \$12,276 or more per year, upper middle income = \$3,976 - \$12,275 per year, lower middle income = \$1,006 - \$3,975 per year, low income = \$1,005 or less per year). Source: Economic Research Service



## Are Speculators Bad People?

The classic definition of a “hedger” is simple. It is someone that either owns a commodity or needs a commodity and wants to know what the price is going to be when they either sell or buy that

commodity at a future date.

A farmer expects to harvest 5000 bushels of wheat three months from now. But, he would like to know right now what he is going to be paid. At the same time, there is a miller that wants to know how much he is going to pay for wheat later on in the year. Neither knows the other party. So the farmer sells an obligation to deliver 5000 bushels of wheat in three months and the miller buys the right to take delivery. Both are hedgers.

There is a clear value and business need that make futures markets important to a smoothly functioning economy. It is to provide certainty for businessmen that

buy and sell items with prices that can fluctuate widely. The alternative would be uncertainty and erratic prices.

The practical problem is that there are not enough farmers and millers to quickly and efficiently make matches and satisfy everyone.

This critical problem was solved centuries ago and that solution is as good today as it was then. It is to offer standard contracts (size, quality, time, place) and create incentives for non-hedgers to get involved. The incentive is the chance to make a profit, maybe a huge profit by guessing (speculating) on what prices will be in the future. Fortunes have been made (and



## Freight

This is the one area where we are going to break our pledge to not talk about regulations.

Fuel is a huge cost for truckers and one that goes up and down rapidly. Most carriers have a system of a base rate + a fuel surcharge that changes periodically based on average cost of fuel (Available on U.S. Department of Energy web site). When fuel costs go up or down, truck rates adjust.

40%  
of US corn  
consumption

goes to  
biofuel  
production.

Source: USDA

The base freight rate to any location depends on size of the load. The bigger the load, the lower the per pallet rate will be.

More complicated is the supply of drivers. Here is where new regulations are having an impact. Over the last few years, new safety rules have been implemented and diligently enforced. There are new limits on the hours that a driver can work in a day and a week. There are also rules that require a truck driver to pass an

annual physical. Not everyone passes. Conditions like high blood pressure will lead to failing the physical and not being able to drive.

Annual physicals and limits on time behind the wheel are starting to reduce the supply of drivers. If you have ever wondered about all the radio ads for companies trying to hire truck drivers, now you know what that is about. So far, the slow economy is keeping the impact of these changes to a minimum. There are enough truckers to do all the trucking at current rates. When the economy picks up, demand for drivers will increase and costs are likely to rise.

lost) in futures markets from the time of their invention.

Those non-hedgers are called lots of things – many not very nice. Speculator is one of the not nice names. That is because those non-hedgers often appear to drive prices higher or lower than it would otherwise be. Either way, half the hedgers are not happy.

A speculator does not want to own the commodity he is investing in. He just wants to profit as the value of his contract changes. When he decides to take his profits or limit his losses, he makes an opposite transaction and zeros out his obligation.

In recent years, financial institutions with huge sums of money to invest have become active in futures markets. The scale of their involvement moves markets up or down. In the short term, they seem to be able to defy the laws of economics. Prices can go up when they are expected to go down and down when they reasonably would go up. In the longer term, the commodity is worth what someone will pay for it. The speculator that buys high and sells low loses money. Just like you and me.

Futures markets allow participants to lock in prices. They do not guarantee anyone a profit.

## A Chemistry and Biology Primer

At virtually the moment that bread comes out of the oven, the staling process begins. The chemistry is that naturally occurring starches in the flour want to crystalize. As that process progresses, the bread moves from fresh and aromatic to stiff and not pleasant to eat.

In recent years, food scientists have found ways to slow the staling process with enzymes. This is why the bread you buy in a grocery stays soft for so long. Enzymes do not work well when making some specialty and hearth baked items, because “super soft” is not wanted.

Bread stales fastest at about a temperature of 37 degrees. Because of that, it is important to NEVER store bread in a refrigerator. If your bread comes to you frozen, remove product from its box and spread packages out to achieve rapid thawing.

Like staling, mold is the result of a natural process. Mold is in the air and bread is a wonderful place for it to grow. Bakers work hard to have an almost aseptic environment when the bread goes in a bag. Almost is not perfect. Whatever little mold is present in that bag will start growing and multiplying. Sooner or later, it will be visible.

Proper storage is important to forestall molding. Dry and not too hot is what you want. Stay clear of heat sources like ovens or stoves. Refrigerators would seem to be a solution, but it is not. Condensation tends to occur in the bag and actually speed the growth of mold.



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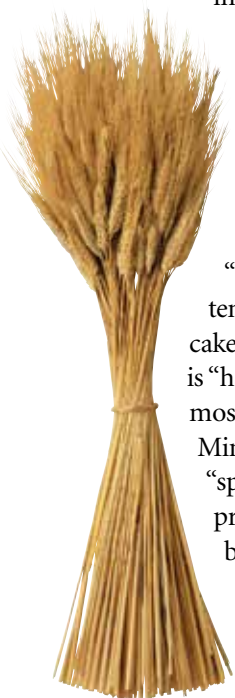
## USEFUL INSIGHTS FOR FOOD SERVICE



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### Why Have Three Major Wheat Futures Markets?

There are three major wheat futures markets in the USA for wheat used in bread and cakes. (Chicago, Kansas City and Minneapolis) They trade different types of wheat. Chicago wheat is "soft." It is ideal for tender products like cakes. Kansas City wheat is "hard." It is ideal for most bread and roll items. Minneapolis wheat is "spring." It is ideal for products like hearth breads where extra gluten strength is needed.



### Who is Ottenberg's Bakery?

We are a 140 year old bakery, still owned and run by the Ottenberg family. We have the scale of operations and operational controls necessary to meet the needs of the largest, most demanding customers. As a family business we act quickly and forcefully to meet customer needs. We serve the food service industry through fresh and frozen distributors in the Eastern US. For more information, please go to [www.ottenbergs.com](http://www.ottenbergs.com) or call us at 800-334-7264.

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