

CURRENT TRENDS FOR COOPERATIVES

Dr. Roger Ginder
Department of Economics
Iowa State University

AAI Expo '05'
Des Moines, Iowa
January 11, 2005

CURRENT TRENDS FOR COOPERATIVES

- Farm Customer Diversity
- Concentration At Production Level
- Changes in the Traditional Value Chain
- Heavy Pressure on Margins
- Concentration at the Local Input Supply/
Marketing Firm Level
- Changing Grain Utilization Patterns
- Changes in The Corn-Soybean Mix

CURRENT TRENDS FOR COOPERATIVES

- Customers Are More Diverse and Have Different Needs and Expectations
 - Specialization
 - Age Distribution
 - Level of Sophistication
 - Time Horizon In Farming
 - Off Farm Employment and Income
 - **Size of Operation**

CURRENT TRENDS FOR COOPERATIVES

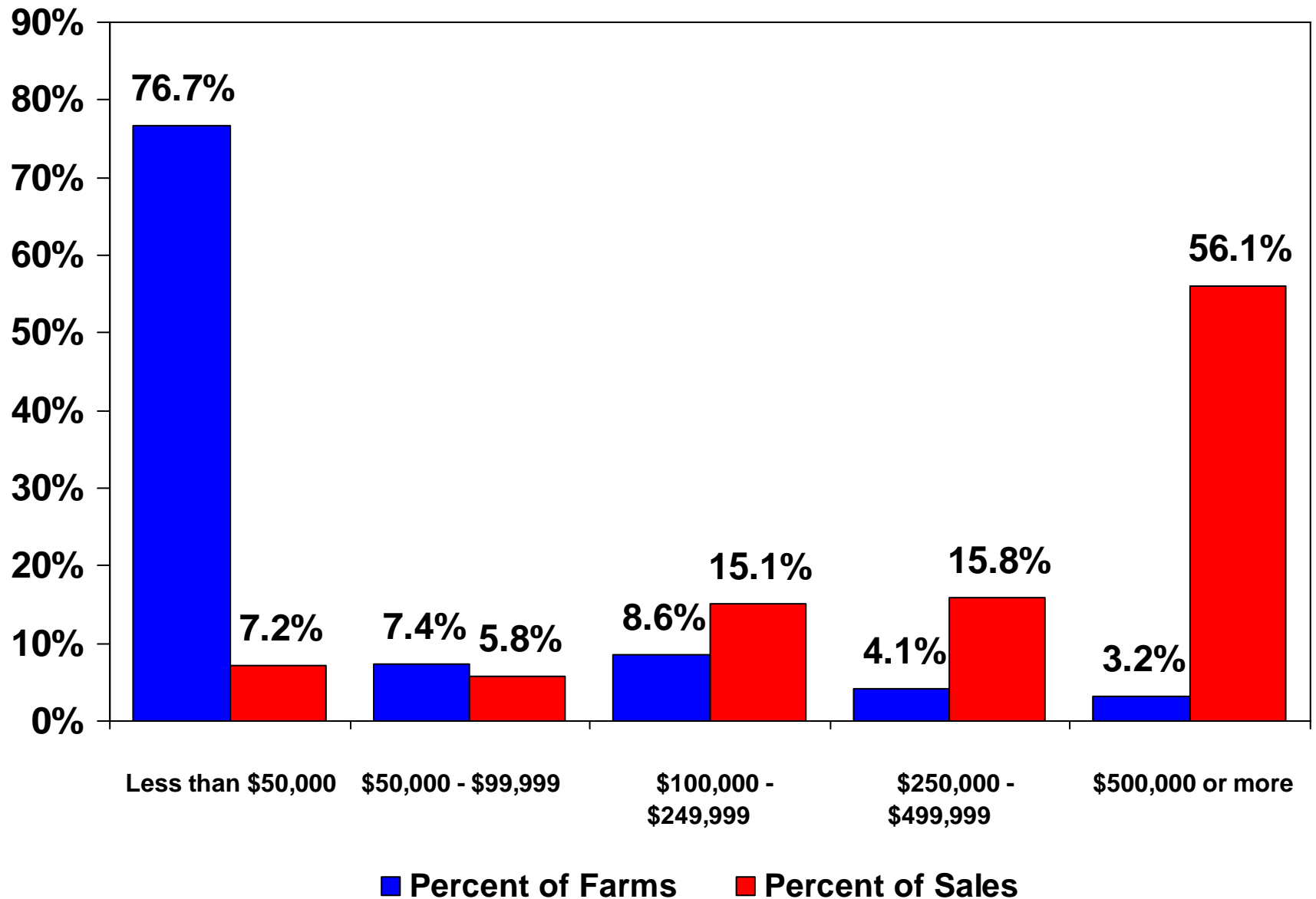
- Concentration is Accelerating in the U.S. Production Sector
 - Larger Scale Operations Account for a Larger Share of the Market
 - Smaller Scale Part Time and “Hobby” Operations Account for Increasing Share of Total Farms
 - Medium Sized Operations Are Disappearing at a Rapid Rate

Gross Sales Categories in Perspective Using Corn Production

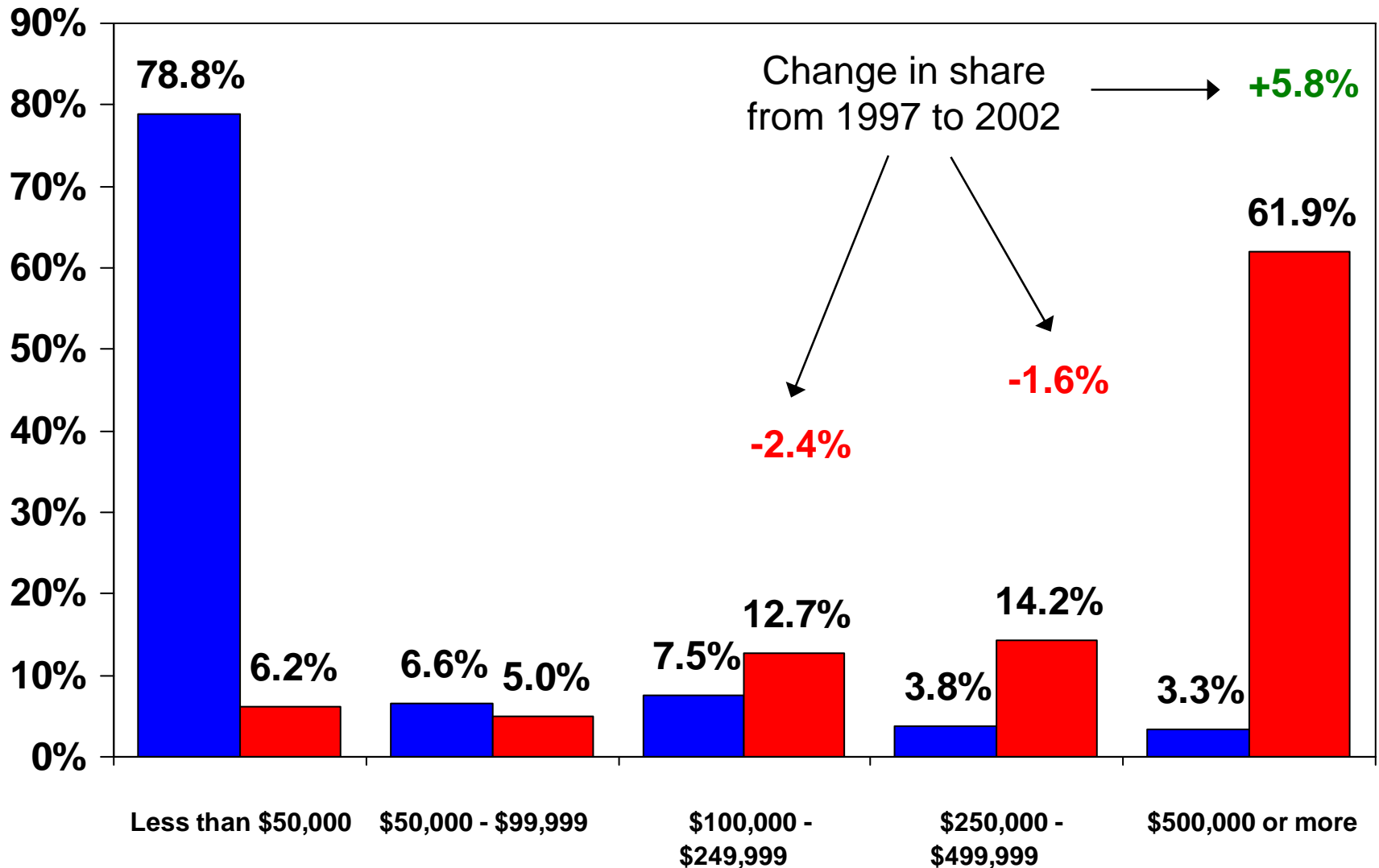
- Gross Revenue Equivalent 200 Bu./A corn @ \$2.00 / Bu. = \$400/ Acre

- \$50,000 Sales Approximates 125 Acres
- \$100,000 “ “ 250 Acres
- \$250,000 “ “ 625 Acres
- \$500,000 “ “ 1250 Acres
- \$1,000,000 “ “ 2500Acres

Distribution of Farms by Sales Category, U.S., 1997



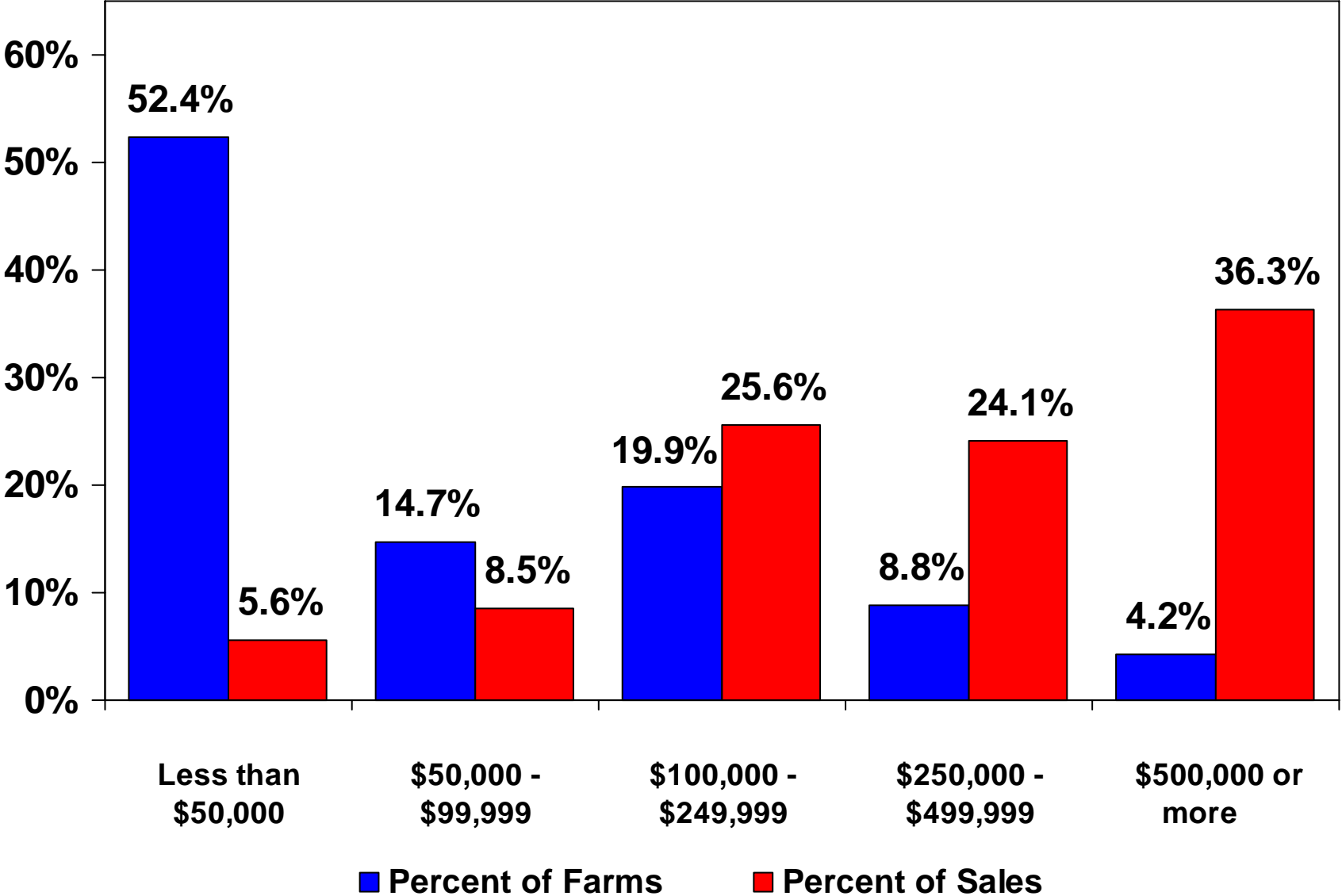
Distribution of Farms by Sales Category, U.S., 2002



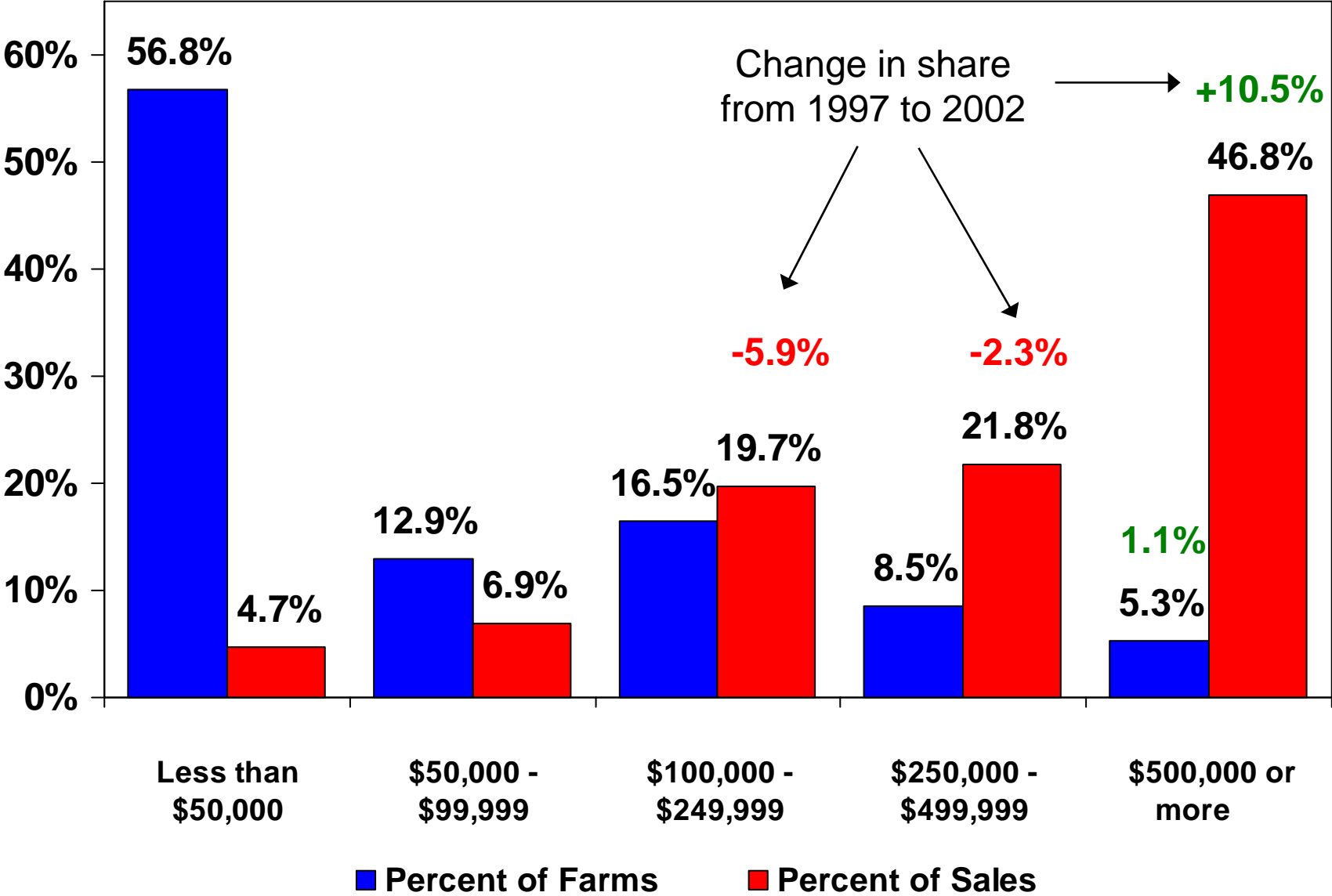
CURRENT TRENDS FOR COOPERATIVES

- Mid-Sized Farm Loss is Less Pronounced in the Iowa Farm Production Sector
 - But Concentration into Farms with Greater than \$500,000 in Annual Sales is Accelerating
 - Medium Sized Operations Are Disappearing at a Rapid Rate
 - These Medium Sized Operations Have Traditionally Been the “Bread and Butter” for Local Farm Input Suppliers and Output Marketers

Distribution of Farms by Sales Category, Iowa, 1997



Distribution of Farms by Sales Category, Iowa, 2002



The Concentration Now Occurring at the Farm Level Is Driving Other Changes in the Input Supply and Grain Marketing Sector

CURRENT TRENDS FOR COOPERATIVES

- The Value Chain is Repositioning on Both the Input Supply and the Product Marketing Sides
 - Farmers Have Purchased Used Semi's
 - Direct Movement of Inputs to Producers
 - Direct Origination of Grain from Producers
 - Blurring of the Traditional Distinctions Between Wholesale and Retail

CURRENT TRENDS FOR COOPERATIVES

- New Structural Arrangements Among Players at Both the Wholesale and the Retail Level
 - Agrilience in Fertilizer and Crop Protection
 - AGM Joint Venture Dissolved
 - New Bunge Joint Venture with Agri-Industries
 - CHS Regionalization Program in Northern Plains
 - AGP Partnerships with Local Coops
 - LOL Joint Ventures with Locals in Feed Mills
 - Ag Partners Joint Ventures Between Cargill and Local Coops and Private Elevators

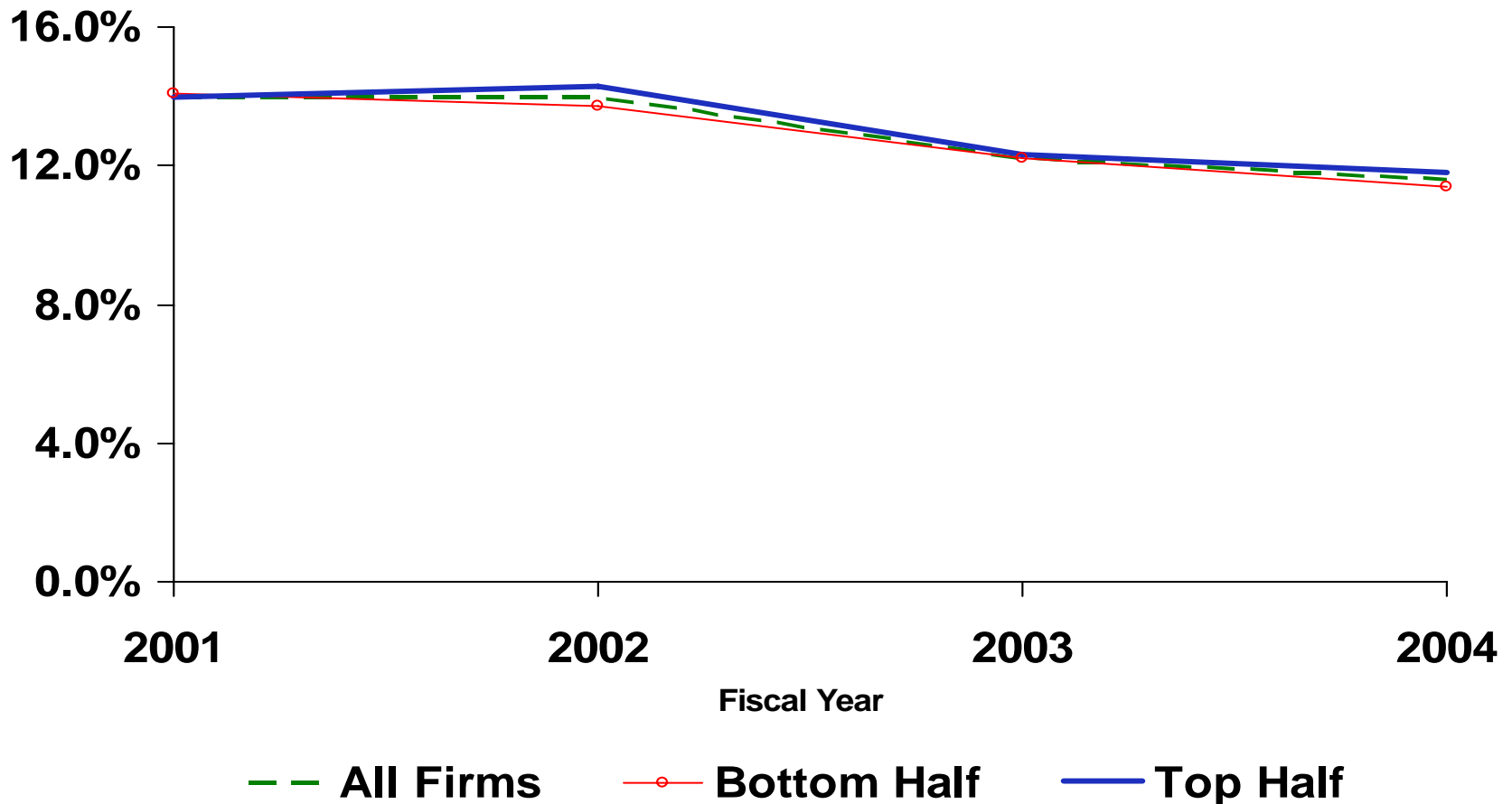
CURRENT TRENDS FOR COOPERATIVES

- Pressure on Gross Margins is Impacting Almost All Local Input Supply/Mkt. Firms
 - Cost of Goods Purchased for Resale
 - Selling Prices to Customers
 - Average Margins per Dollar of Sales and Service Income Fell From 14% in 2001 to 11.6% in 2004 (A Margin Reduction of 17%)
 - Price Pressure from Larger Customers and Larger Suppliers Squeezing from Both Sides

Overview

- The sample consists of 64 cooperatives in Iowa with data from 2000-2004
- Fiscal years used run from September 1 through August 30. For example, FY04 spans Sept. 1, 2003 through August 30, 2004.
- Firms were sorted by FY04 local* profit before taxes and classified as being in either the top half or the bottom half of the sample, based on this criterion.
- Highest Level of Local savings for the bottom was approximately \$150,000.

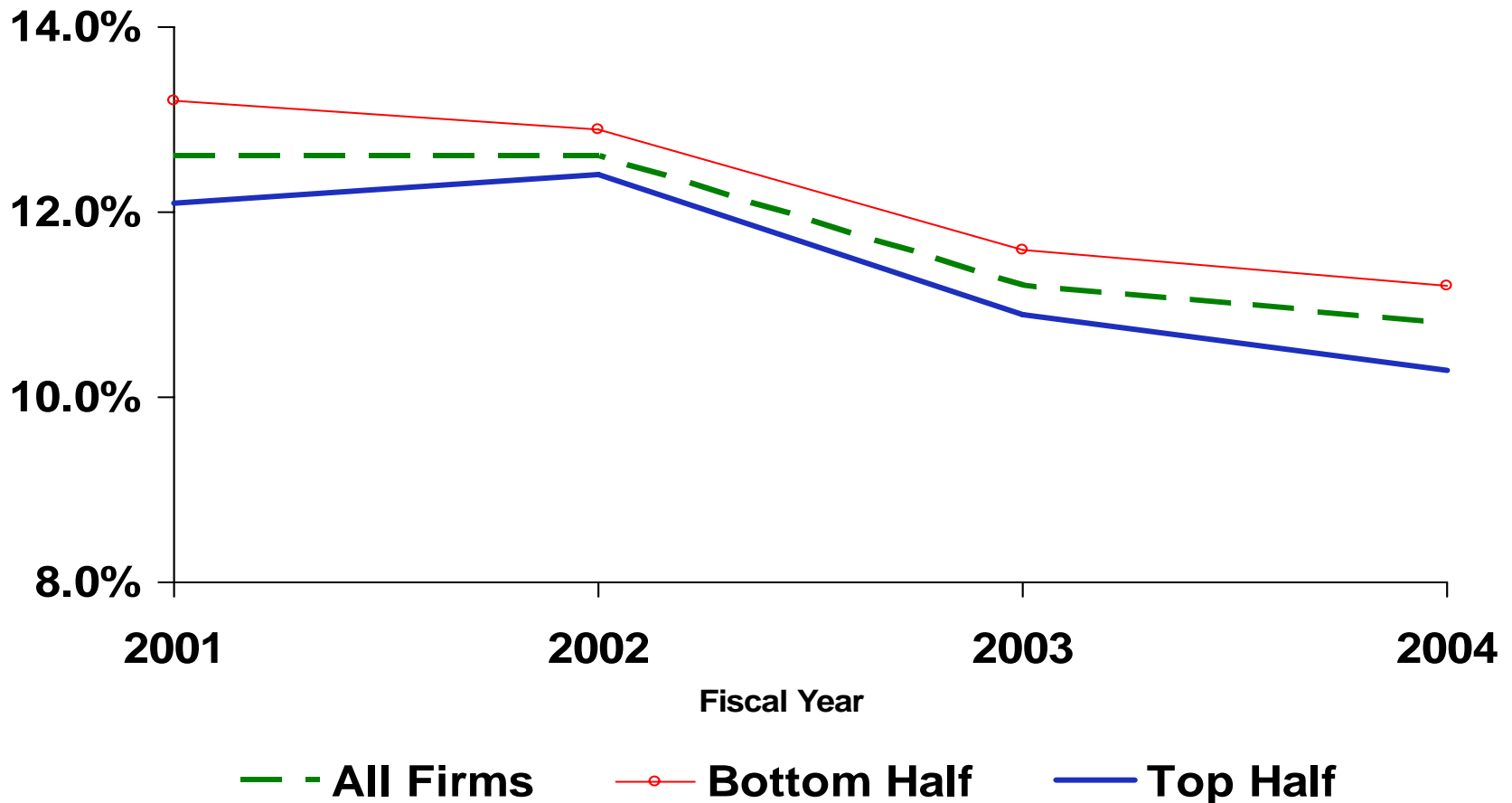
Average Gross Income as a Percent of Sales & Other Income



CURRENT TRENDS FOR COOPERATIVES

- Local Supply and Marketing Firms Are Pursuing Several Strategies to Adjust
 - Some Are Closing (Or Seasonalizing) Marginal Facilities With High Unit Costs
 - Most Are Attempting to Reduce Labor Expense where it is Possible
 - Larger Firms are Automating Farm Supply and Grain Marketing Activities to Reduce Labor Costs per Unit
 - Most Are Making Reinvestment and Upgrading Decisions More Carefully
 - Most Are Seeking to Parse Expenses Everywhere They Can

Average Total Expense as a Percent of Sales & Other Income



CURRENT TRENDS FOR COOPERATIVES

- Average Expenses Per Dollar of Sales and Service Income Fell From 12.6% in 2001 to 10.8% in 2004 (Approx. 14%)
- The Average for Firms in the Least Profitable Half fell from 13.2% to 11.2%
- The Average for Firms in the Most Profitable Half fell from 12.1% to 10.3%

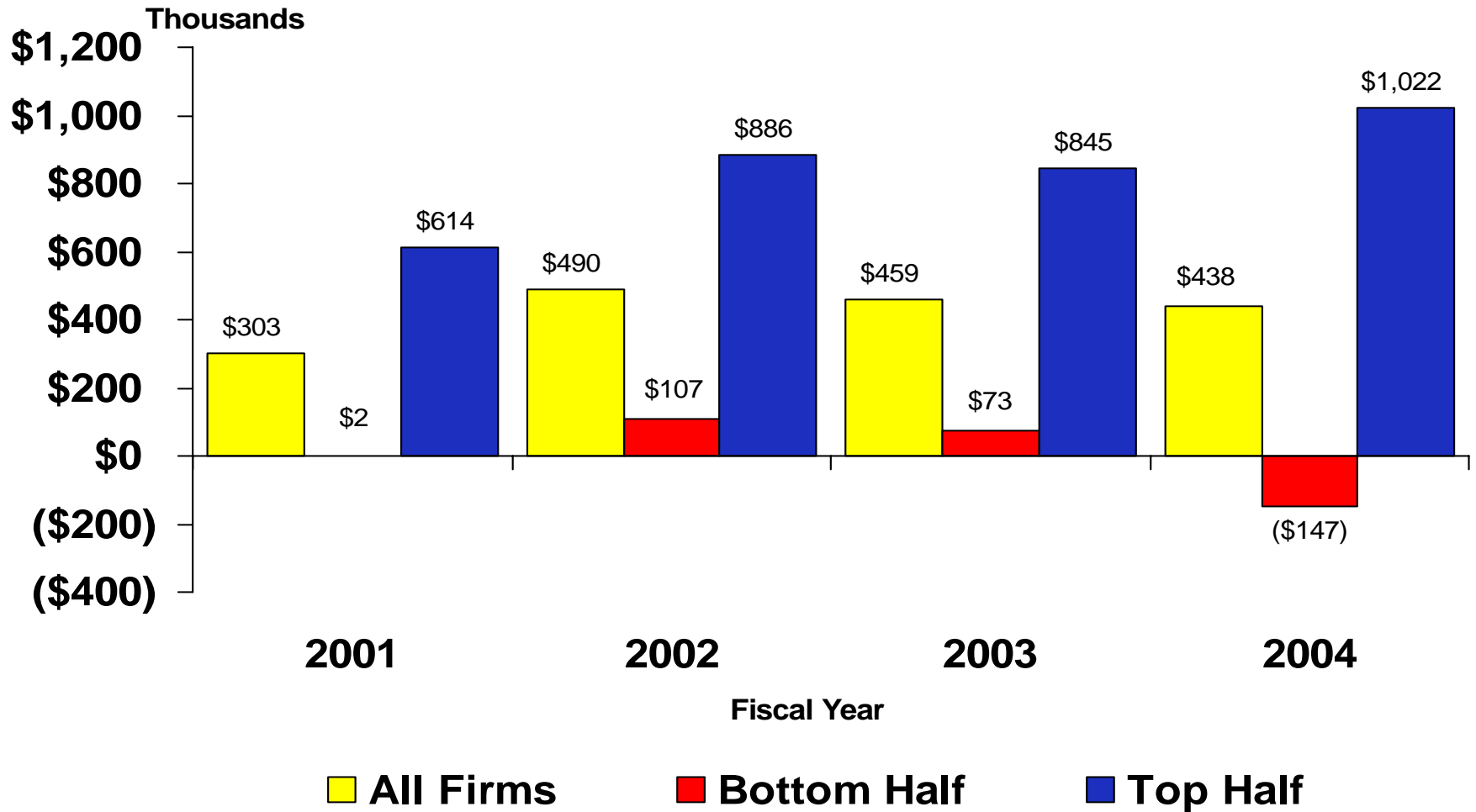
CURRENT TRENDS FOR COOPERATIVES

- Cutting Expenses in This Industry is ***Very Difficult***
 - Many Expenses Are Fixed and Do Not Change with Volume
 - Others Such as Interest, Insurance and Retirement Are Difficult to Control Directly
- The High Level of Fixed Expense and Uncontrollable Expenses Make Profitability Highly Volume Dependant

CURRENT TRENDS FOR COOPERATIVES

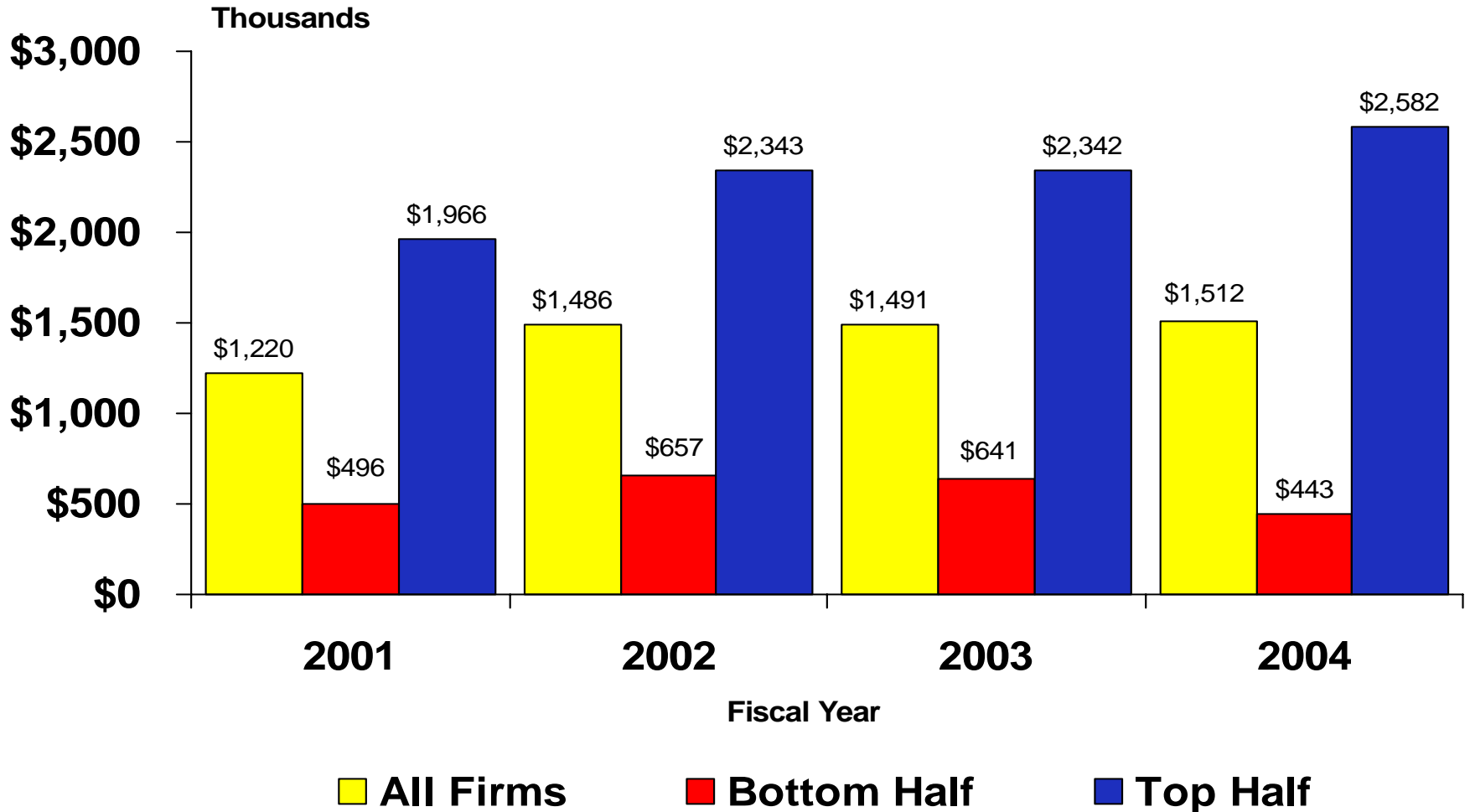
- Firms in the Least Profitable Half of the Sample Are Being Starved For Cash
 - Low Earnings Due to the Margins Squeeze
 - Difficulty in Maintaining Fixed Assets and Financing Growth

Average Local Profit (Savings) Before Tax



Local profit (savings) excludes refunds from other organizations.

Average Local Cash Flow



Local Cash Flow = profit before tax - refunds from other organizations + depreciation

CURRENT TRENDS FOR COOPERATIVES

- The Concentration at the Producer Level Coupled with the Margin and Expense Pressure Have Created Concentration at the Retail Level in the Farm Input Supply and Marketing Industry
 - Need Bargaining Power With Wholesalers, Vendors and Farm Customers
 - Need Larger Volumes of Sales to Cover Fixed and Uncontrollable Expenses

2004 Iowa Averages For Sales, Fixed Assets and Equity – 64 Firms

	Sales	Fixed Assets	Equity
<u>Concentration</u>	<u>(\$ Mil)</u>	<u>\$ Mil</u>	<u>(\$ Mil)</u>
Top 10	195.6	21.8	31.0
Top 15	166.5	18.0	26.9
Top 20	148.0	15.5	23.6
Top 25	132.3	13.5	20.9

Estimated Concentration of Sales, Fixed Assets and Equity – 64 IA Coops, FY04

<u>Concentration</u>	<u>Sales</u>	<u>Fixed Assets</u>	<u>Equity</u>
Top 10	44%	49%	42%
Top 15	57%	60%	54%
Top 20	67%	69%	63%
Top 25	75%	76%	70%

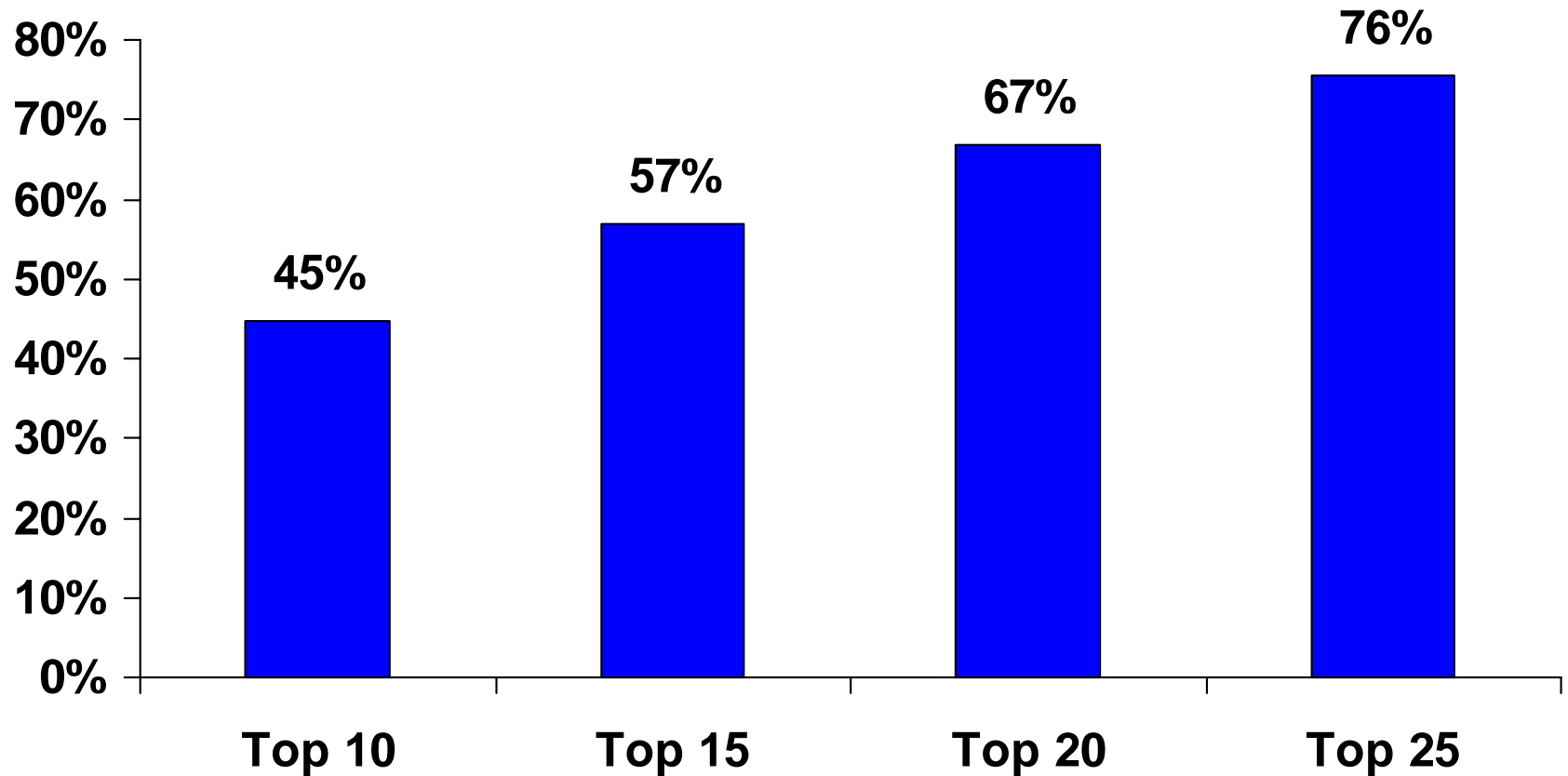
2004 Iowa Averages For Sales, Fixed Assets and Equity – 64 Firms (Averages by Size Category)

Concentration	Sales (\$Mil)	Fixed Assets (\$Mil)	Equity (\$Mil)
Top 10	203.1	20.5	30.0
Top 15	172.8	17.6	26.4
Top 20	153.3	15.1	22.8
Top 25	137.0	13.3	20.5

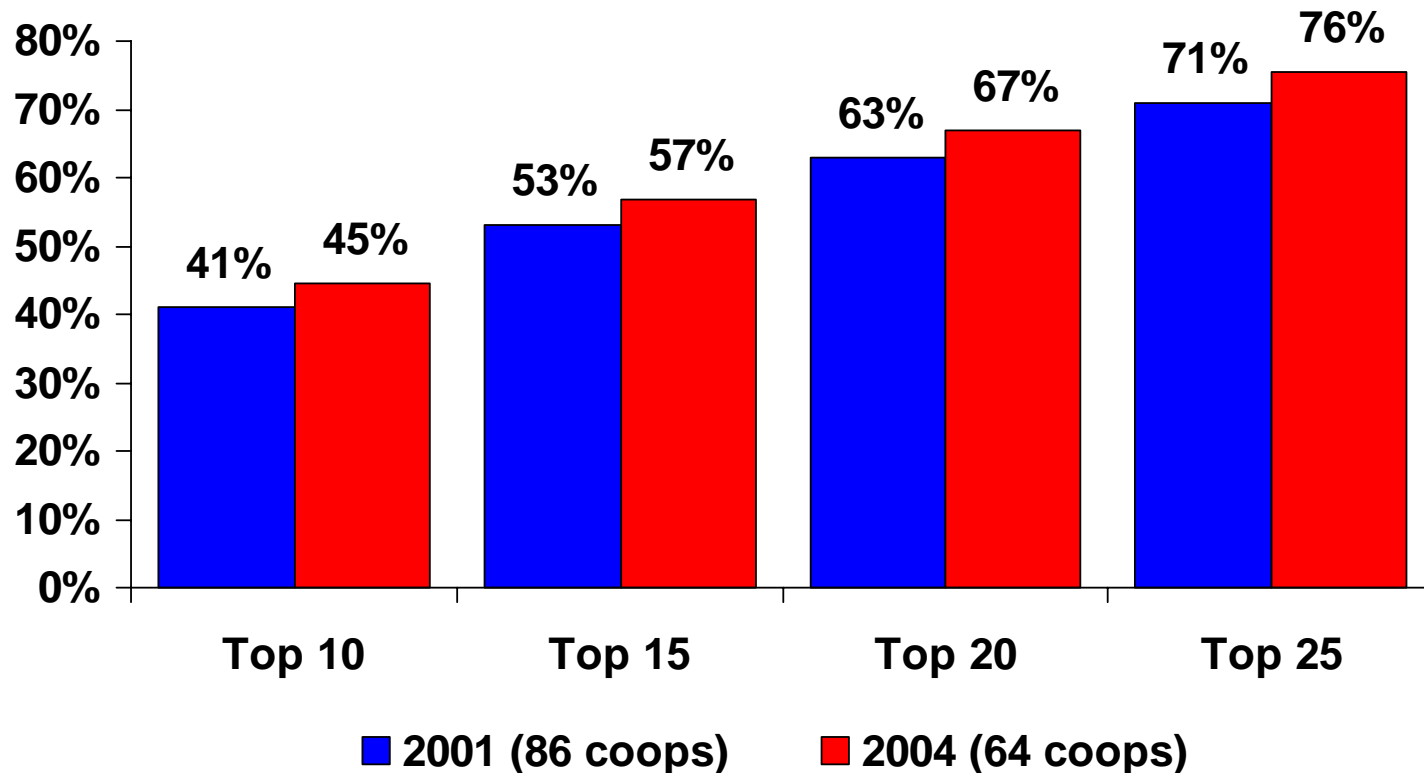
Estimated Concentration of Sales, Fixed Assets and Equity – 64 IA Coops, FY04

<u>Concentration</u>	<u>Sales</u>	<u>Fixed Assets</u>	<u>Equity</u>
Top 10	45%	47%	41%
Top 15	57%	60%	54%
Top 20	67%	68%	62%
Top 25	76%	75%	70%

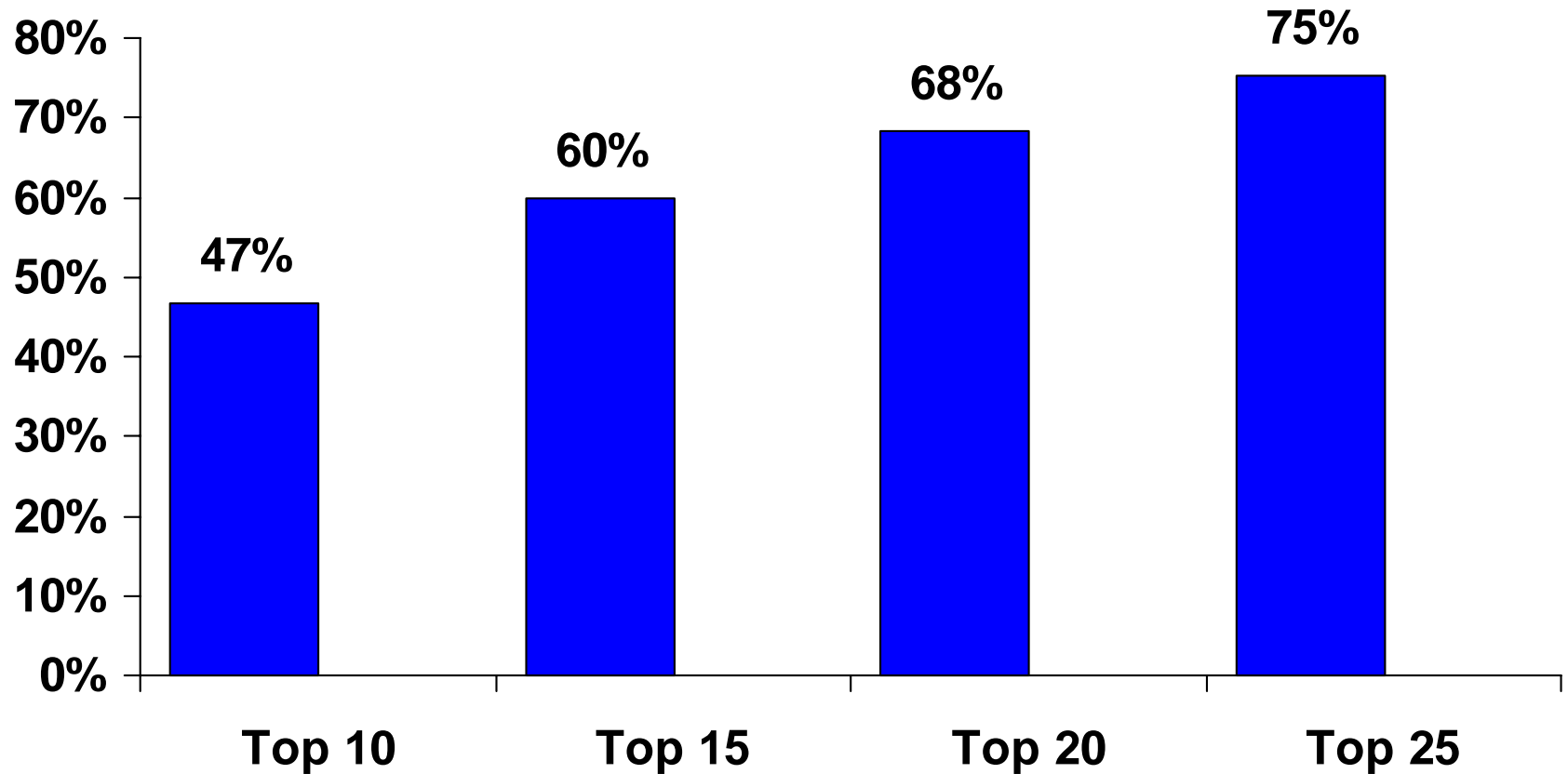
Estimated Concentration of Sales 2004 – 64 Firms



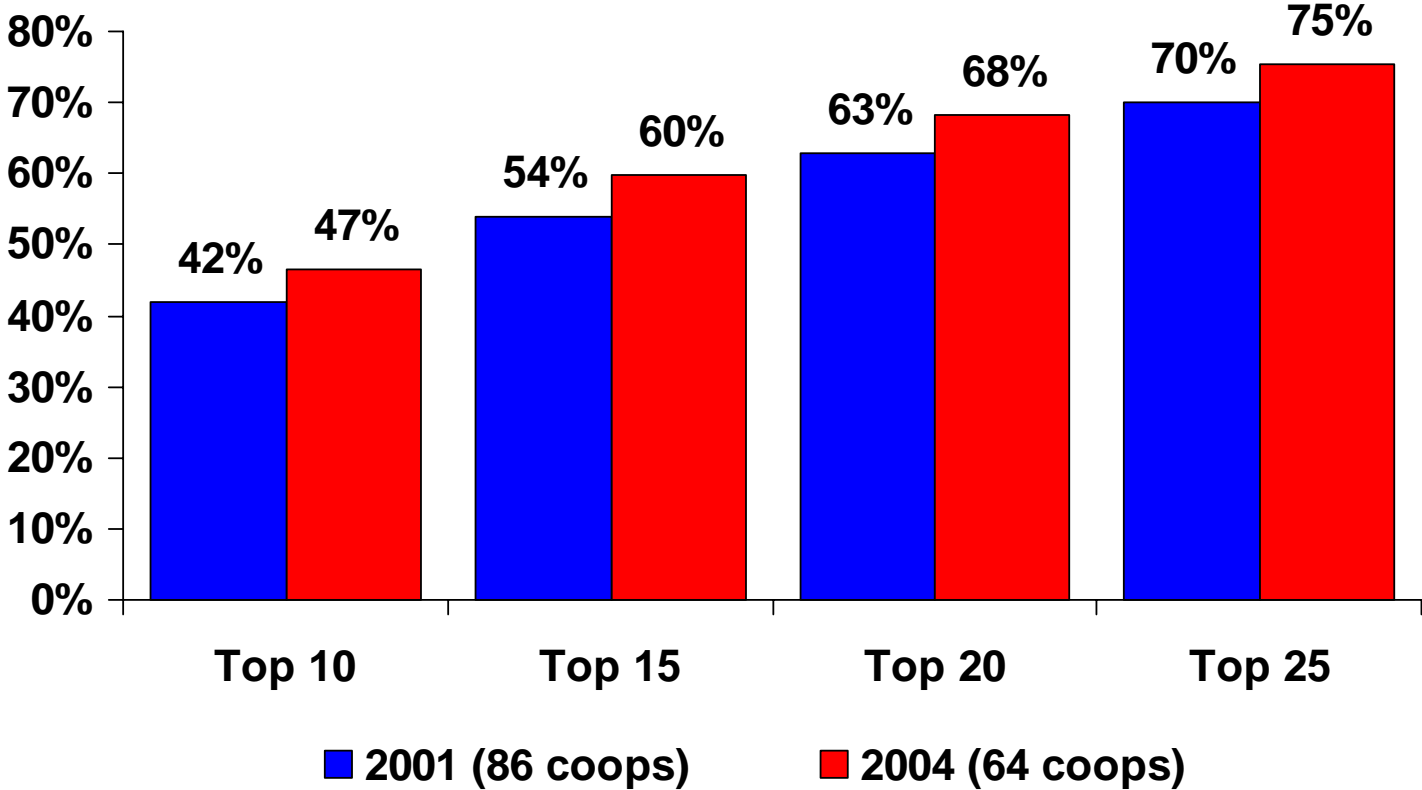
Estimated Concentration of Sales 2001 vs. 2004



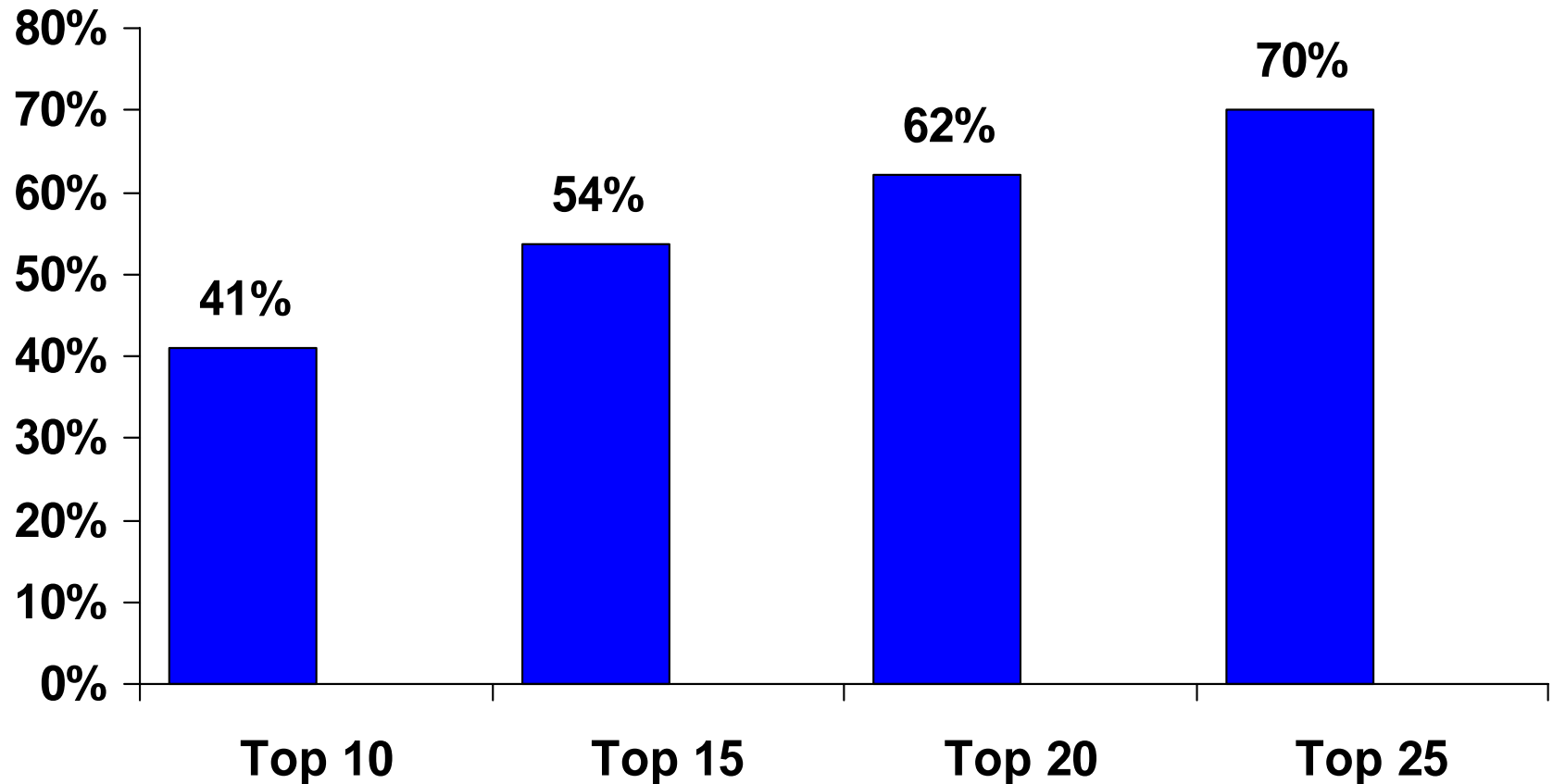
Estimated Concentration of Fixed Assets 2004 – 64 firms



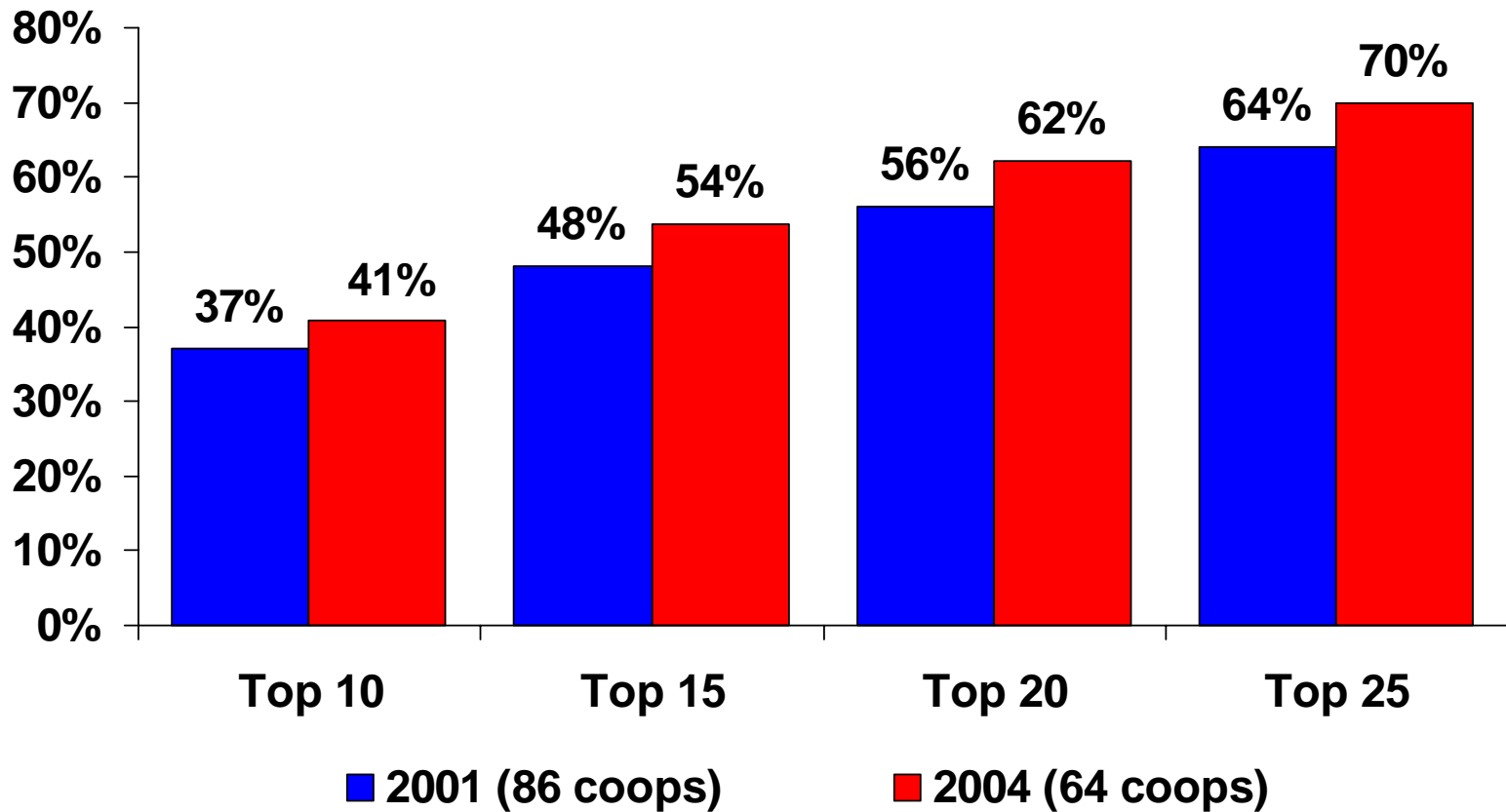
Estimated Concentration of Fixed Assets 2001 vs. 2004



Estimated Concentration of Equity 2004 – 64 Firms



Estimated Concentration of Equity 2001 vs. 2004



CURRENT TRENDS FOR COOPERATIVES

- Changing Grain Utilization Patterns are Emerging
 - More Grain Moving to Processing—especially Ethanol
 - Larger Fraction of the Grain Used For Domestic Feed Manufacturing Moving to Integrators
 - Greater Competition Among Processing, Feeding and Export For Existing Supplies

CURRENT TRENDS FOR COOPERATIVES

- Changing Grain Utilization Patterns are Emerging
 - Facilities In Some Areas Are Facing Heavy Competition for Export Grain and Grain For Domestic Livestock Feed Markets
 - Programs To Originate Grain For Ethanol Plants is Becoming More Important
 - More Elevator Storage Capacity is Used to Serve Ethanol Markets Than Traditional Markets

CURRENT TRENDS FOR COOPERATIVES

- Changing Grain Utilization Patterns are Emerging
 - New Strategies Will Need To Be Developed to Deal With the Increased Demand from New Capacity Now In Production
 - Additional Plants Are in Planning Stages or Under Construction
 - De-germing May Be a Possibility

CURRENT TRENDS FOR COOPERATIVES

- Some Believe That a Modest Shift In The Traditional Corn Soybean Acreage Split Will Be Occurring in the Future
 - Dramatic Increases in Corn Yields
 - Herbicides to Permit Corn on Corn
 - Increasing Production Competition From South America
 - Asian Rust Identified in U.S.
 - Still Uncertain If It Will Occur and If So How Large It Will Be

CURRENT TRENDS FOR COOPERATIVES

- Likely Impacts of A Shift From Traditional Corn Soybean Acreage Split
 - Larger Bu. Volumes to Be Handled
 - Increased Demand For Plant Food Product
 - Possibly Increased Crop Protection Product
 - Reduction in the Supply Gap Resulting From Increased Corn Use in Ethanol Production
 - More Difficulty in Meeting Harvest Time Glut

QUESTIONS?