Iowa State University

Extension and Outreach / Department of Economics

Consolidation Trends Among Ag Co-ops

Economics and Agriculture

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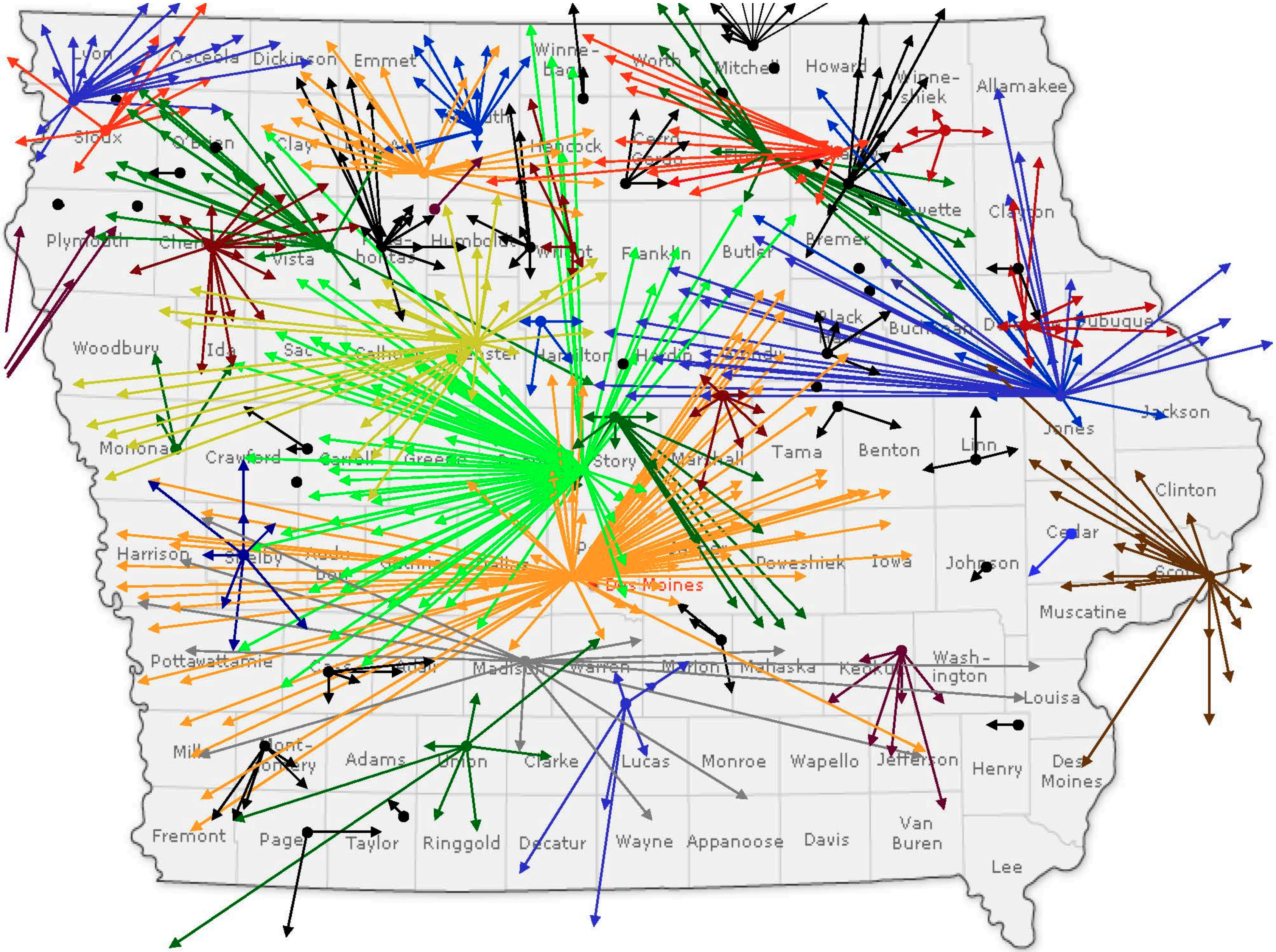
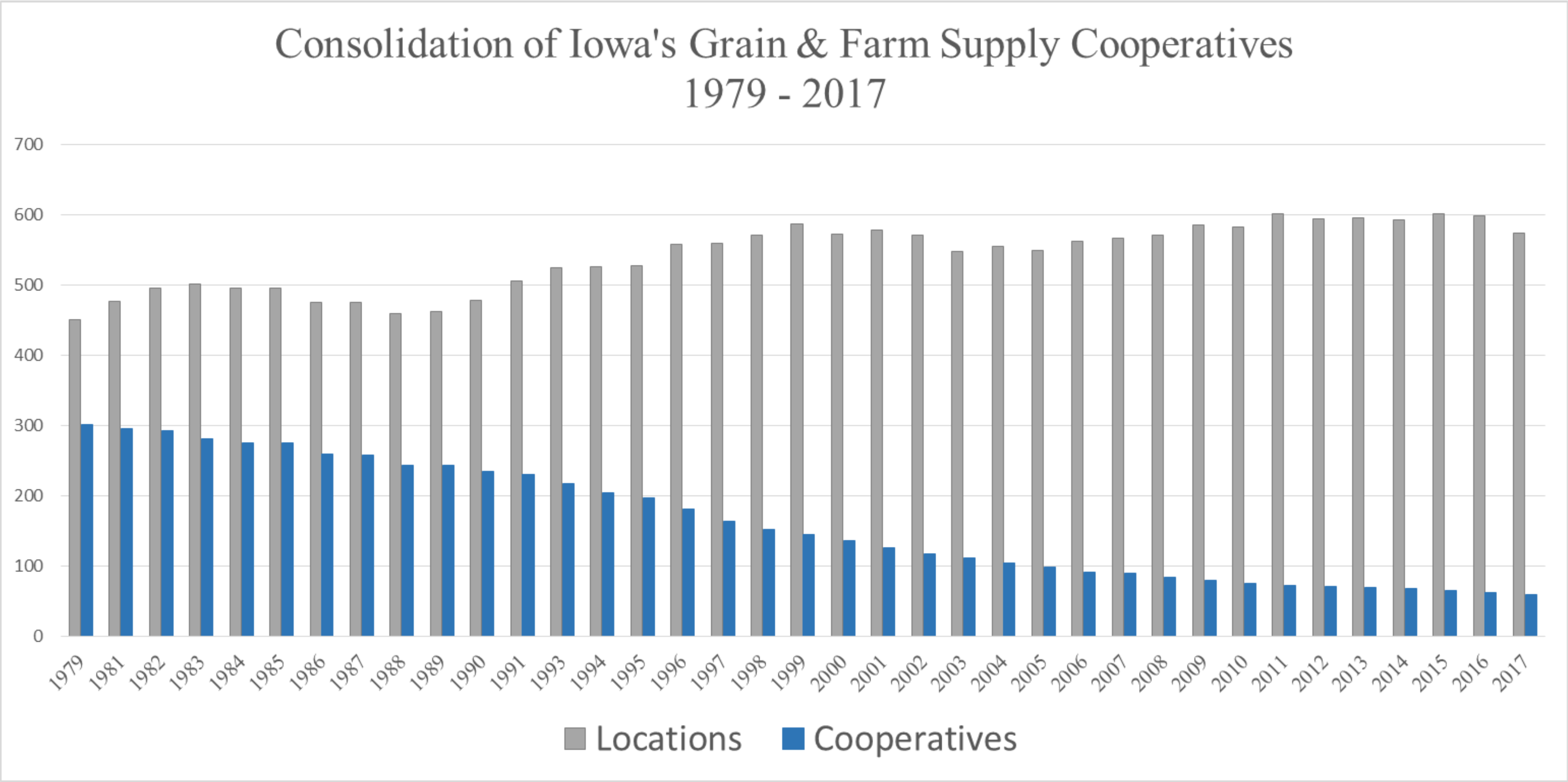
Trends Challenging Leadership

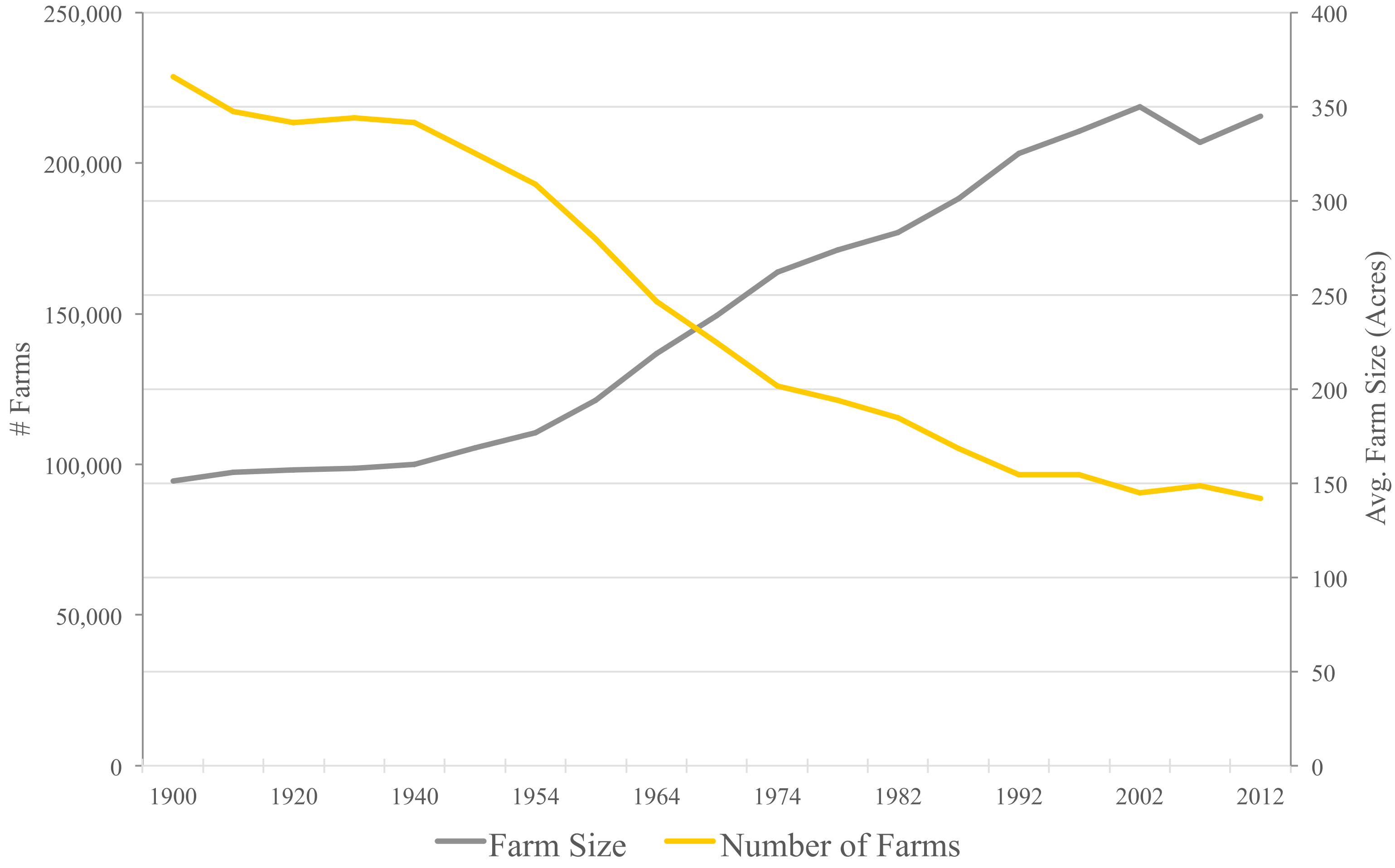
- Evolving supply chains
- Increased diversity of producers
- Human capital drivers
- Creating a clear value proposition to members



Source: Iowa Institute for Cooperatives, 2016


Consolidation of Iowa's Grain & Farm Supply Cooperatives
1979 - 2017
700
600
500
400
300
200
100
0
1979 1981 1982 1983 1984 1985 1986 1987 1988 1989 1990 1991 1993 1994 1995 1996 1997 1998 1999 2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017
Locations
Cooperatives

Iowa's Producers Are Getting Bigger



Data Source: National Ag Statistics Service, USDA

Co-op “Partners” Are Getting Bigger

- Bayer – Monsanto
- Dow – DuPont
- ChemChina – Syngenta
- John Deere
- Agrium

What Are The Justifications by Co-ops in Iowa?

- Enhanced cost efficiency in admin and operations (economies of size)
- More ‘output’ with fewer inputs (economies of scale)
- Access to strategic assets (location specificity)
- Access to talent
- Value creation in the eyes of producer-members

What About Beyond Iowa?

Kansas

- 74 g&fs, approximate 588 branches
- Retiring managers a catalyst
- Co-ops bypassing merger vote through L.L.C. structures
- How will they deal with governance issues?

Minnesota

- Most g&fs are 1 – 3 locations
- Uptick in mergers but some voted down
- Farmers value choice of doing business with many co-ops
- Managers see clear ‘back office’ and safety cost savings and talent acquisition by merging
- Energy co-ops: risk, and difficult to scale up to get cost efficiencies

What About Beyond Iowa?

Missouri

- Landscape dominated by MFA, Inc. (100, of which approx. 24 are independent)
- 20 – 25 independent local g&fs – most 1 location
- Very few ‘super locals’
- Increased importance of non-member business to generate permanent equity

Oklahoma

- < 40 co-ops, merger is a big topic
- Financial stress (severe droughts, infrastructure issues)
- Cotton profitability driven by volume
- Grain alliances are major part of landscape (Equity Marketing Alliance merger with CoMark, L.L.C.)

Supply Chains in Ag: My Thoughts

- A supply chain is itself a “thing” - a collection of individuals, firms, resources, relationships, information, technology, etc – that changes with influence or pressure.
- Each product and service has its own supply chain, the demands of one chain (e.g. grain) are inherently different than those for another (e.g. energy).
- A co-op manages several supply chains simultaneously; Retailers are on competing ‘links’ in a supply chain.
- An ‘effective’ supply chain is one that will reduce costs – accounting and economic costs – associated with moving the product or service from producer to consumer.
- Co-ops who merge may gain access to a preferential place in the chain, or a new chain entirely.
- There are non-merger options to achieve these: alliances, contracts, JVs, L.L.C.s

Horizontal versus Vertical?

Horizontal

- Acquiring 'like' processes at the same level of the supply chain
- Why: size, reduce competition, economies of scale, gain access to new markets/customers, influence with other levels in chain

Vertical

- Acquiring processes/production at a different level of the supply chain
- Why: capture margins along supply chain (bring value in-house), reduce costs, control supply chain (transaction costs), influence different levels in chain

What Does This Matter?

- Co-ops are jockeying for their position on the links for each of grain, agronomy, energy, feed, and others.
- Supply-chain challenges are coming from many angles.
- Co-ops are looking for combinations of vertical and horizontal arrangements to solidify or improve their footing, but members may perceive only the horizontal move, the vertical is more nuanced.
- Managing the supply chain may put the producer and co-op at odds.

Do members correctly identify with the motives and strategy?

Principal-Agent Framework

The principal-agent model recognizes the costs and potential inefficiencies that arise when one party is charged with acting on behalf of another and goals, preferences, information, and risk appetites are not aligned.

Members: Principals

Board Members: Principals and Agents

Manager: Agent

Co-op Value

- Price and market functions
- Patronage
- Service
- Existence Value
- Governance
- Community

How does consolidation / merger change these?

The Crux

Consolidation is fundamentally putting at odds members' values and perceptions with leaderships' values and perceptions.

- "The co-op is just another big business."
- "It's not my co-op anymore."

The frictions created through consolidation are not pecuniary, but have significant financial ramifications.

Underlying Issues

- Members perceive value is being assigned to one segment of producers
- All producers share in the provision of value
- Free riding
- Horizon problem
- Membership heterogeneity
- Disconnect between shareholders and leadership

IMHO, THE most important function of the members' cooperative is not being raised high enough in this conversation.

Solutions

A re-alignment of principals and agents though:

- Education
- Strategy buy-in
- Transparent value proposition
- Culture change
- Change management; finding common ground

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