Understanding Your Business Environment

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Co-ops were a part of YESTERDAY’S food and fiber system...

What will their role be in TOMORROW’S food and fiber system?

Cooperative Board Members Should be Aware of Issues and Trends Involving:

- Their customer base
- Ag Service Industry
- Cooperative industry
- Auditing and accounting standards
Changing Customer Base

- Fewer but larger farms

Farmers are getting larger equipment

More Differences Between Farms

21st Century Farms

- Commercial Operator
- Traditional
- Lifestyle

Commercial Farms

- 10,000 to 50,000 acres
- Multiple families/investors
- Rent/lease/control assets
- Deal with large suppliers
Traditional Family Farms
- $150,000 to $600,000 in revenue
- Last generation of family farm
- Seeking economies of scale
- Focus shifting to transition management

Lifestyle Farms
- Off farm employment
- “Sundowner” farmer

Also includes higher income
“work in town and live in country” customers

One Size May Not Fit All
- Different locations have different needs
- Volume discounts
- “discount version” or “full service”
- Bidding for business
Cooperative Retail Stores Are Changing

Oklahoma Cooperatives Are Investing in New Retail Locations

Changing Fertilizer Industry
- Shift to off-shore production
- Increased price volatility
- Emerging issues:
  - Warehousing
  - Forward pricing
**Fertilizer Environment**

- 1980
  - Domestic production
  - $2.50 natural gas
  - Continuous supply
  - Priced for the season
  - $20/ton risk
- 2005
  - Offshore production
  - $13.00 natural gas
  - Planned supply
  - Daily pricing
  - Contract enforcement
  - $200/ton risk

**OSU Fertilizer Warehousing and Application Research**

- $24/ton to cover warehouse cost
- $3.60/acre to cover application costs
- Very significant economies of scale in warehouse construction
- Applicator transport time may offset economies of centralized warehouse

**Cooperatives Operate in a Rapidly Changing Industry**

- Consolidation
- Streamlining to increase efficiency
- Investing to serve new customers
Number of Co-ops – CHS & Land O Lakes

Return on Equity

Bigger Can Be Better
## Other Ways to Improve Efficiency
- Alliances
- Cost Control
- Improved marketing
- Exiting unprofitable areas

## Measuring Costs: Profit Center Analysis
- Understand the profitability of each product line
- Understand the profitability of each customer group
- Measure the returns against benchmarks
- Determine the challenges and opportunities across product lines and locations

## Measure Costs and Returns at an Actionable Level

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<th>GRAIN</th>
<th>AG SUPPLY</th>
<th>STATION</th>
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Expense Ratios by Location

Profit Center Analysis Allows You to:
- Focus on your winners
- Cut costs and improve efficiency
- Outsource sub-performers
- Shoot your dead horses

OSU Financial Ratio Analyzer
Focusing our Marketing Efforts

- 20% of the customers account for 80% of the volume
- Focus on the customers that will be 80% of your business in 5 years
- Determine the products and services needed
- Become the least cost supplier for the products and services offered

Customer Segmentation

- Identify grower segment and characteristics
- Monitor volume trends by segment
- Product/Service bundle designed to meet grower needs
- Differential pricing based on costs and price sensitivity
- Monitor account performance and profitability

Example: Cooperative ABC

- Accepted just over 3,000,000 bushels of wheat from 307 customers.
- Sold 8,500,000 total pounds of fertilizer from 167 customers.
- Members hold $2,000,000 in equity in the cooperative.
Who holds the largest share of cooperative sales

- Distribution of Wheat Income
  - Q1: 4%
  - Q2: 8%
  - Q3: 17%
  - Q4: 71%

- Distribution of Fertilizer Income
  - Q1: 20%
  - Q2: 22%
  - Q3: 5%

Customer Analysis

- For the top quarter of wheat customers (76) 51% do not buy fertilizer with the coop.
- 36% are in the top quarter of fertilizer customers.
- 14% buy fertilizer from the cooperative but are not in the top quarter of fertilizer customers.
- Where is the rest of the fertilizer business going?
  - Top Quarter of Wheat Customers vs. their fertilizer quartile

Customer Analysis Allows You to Focus

- Contact 76 large producers an asked to win their business
- Recognize 51 loyal key members and work to keep their business
Focused Marketing

Key Accounts

Fertilizer

Wheat

Supply

Focus on your key accounts that hold the largest share of business volume.

OSU Market Share Calculator

Accounting Auditing Issues

- Sarbanes – Oxley Act of 2002
- Active audit committee
- At least one financial expert
- Independent directors
- Internal controls to prevent fraud
- Code of ethics
- Whistleblower protection
Equity Issues

- Most cooperatives need additional equity
- Equity supply: fewer young producers
- Equity demand: many aging members
- Is your cooperative equity structure sustainable in the long-run?

Equity Alternatives

- More timely equity redemption
- Alternative equity redemption systems
- Outside equity
- Dividends on owner capital
- Shift to unallocated equity
- Non-patronage
The Future Isn’t What it Used to Be

Success in today’s environment depends on the ability to envision the future and get there first!
John E. Gherty CEO, Land O’Lakes

Change is optional.
Survival is not mandatory!
Peter Drucker
Business Analyst and Author

Other hockey players skate to where the puck is.
I skate to where the puck will be.
Wayne Gretsky, Hockey Star

Cooperatives Are Changing

- Redesigned systems
- Measure and cut costs
- Entering new markets

Cooperative Values Haven’t Changed

- Democratic control
- Customer owned/customer benefit
- Cooperation among cooperatives
- Concern for community
Successful Cooperatives

- Vision and Mission
- Outstanding Management and Boards
- Efficient
- Understand Changing Customer Base
- Alert to New Opportunities

Cooperatives Matter
It’s a Great Time to Be a Cooperative Board Member

Thank you for your attention