Rural COOPERATIVES

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A Sea of Greens

Low-income farmers use vegetable processing, marketing co-op to create new opportunity in north Florida

Planning to Prosper:

Recalling lessons learned from livestock slaughter and meat packing co-ops

"Many farmers and farm groups continue to be interested in handling some livestock through cooperative meat packing plants. This desire to own and operate their own slaughter, processing, and merchandising facilities increases during periods of low livestock prices and small feeding margins."

R. L. Fox
USDA Farmer – Cooperative Service
April 1957

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At the dawn of the 21st century, R.L. Fox's words are no less true than they were 42 years ago. Fox lamented that the farmers' share of the consumers' meat dollar declined from 73 percent in 1946 to 52 percent in 1956. In December 1998, farmers' share of each consumer retail pork dollar had dropped to 12 cents. During the same period, beef producers received 44 to 50 percent of the consumer retail dollar. While beef producers may appear to be in a stronger position than pork producers, note that the 44 percent share at the feedlot gate must compensate cow-calf producers and backgrounders in addition to feedlot-operators.

Increased marketing margins can be partly explained by the addition of consumer-driven characteristics added beyond the farm gate, including such ready-to-cook items as grilling kabobs and marinated steaks. Still, many consumer-desired characteristics are inseparable from the production process, such as leanness, tenderness and flavor. Market-oriented pricing and procurement methods have not always compensated producers for the value of characteristics inherent in genetics or production processes. Cooperative involvement in value-added processing is one method producers can be compensated for the true value of their production.

Recent interest in cooperative slaughter and meat processing among farmers, ranchers and feeders is driven by low prices and smaller profit margins, as well as by significant changes in the structural and institutional environments that have increased risk among independent producers. Recent changes to a more market-oriented federal farm policy have exposed producers to increased price risk. Continued vertical coordination and integration can potentially reduce market access for some producers. While the globalization of markets increases opportunities, participation in these markets also makes U.S. producers susceptible to additional risk.

Randall Torgerson, deputy administrator of the Rural Business-Cooperative Service of USDA Rural Development, summarized the underlying interest in cooperative slaughter and meat processing in an article he wrote for the United Kingdom 1999 Yearbook of Agriculture:

"Two processes are influencing how the food industry is organized and dealing with this marketing margin situation: more integration and coordination. Cooperatively-owned businesses are a natural vehicle for turning these processes into members' benefit. Through joint ownership of marketing, farm input or service assets, cooperatives become the off-farm business — the business beyond the fence line, in an integrated sense. The key is that the driving force behind this integration is the entrepreneurial business unit — the farmers' operation and not some outside dominating force."

Successful cooperative organization

As producers attempt to move closer to the consumer and increase their share of the retail food dollar through the formation of off-farm businesses, they face opportunities and risks. These opportunities and risks differ from those they encounter as producers. To successfully manage these risks, producers need to develop a well-defined organizational plan.

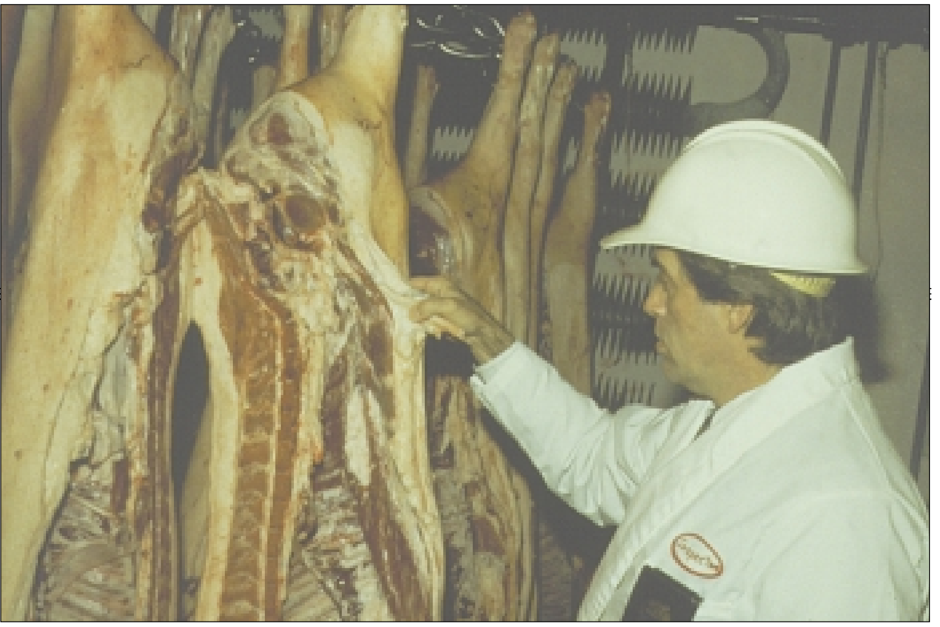
Producers benefit if cooperative strategies take advantage of changes in institutional processes. Careful planning allows producers to effectively recognize risks. Once these risks are identified, the cooperative can develop business strategies that limit these risks to an acceptable level.

In 1996, Galen Rapp and Gerry Ely, USDA cooperative development specialists, codified years of experience in a 16-step sequence for cooperative organizations. The plan may take up to two years to develop and implement, but only after completion of the planning steps should a cooperative commence operations. In "How to Start a Cooperative" (CIR 7, available from USDA Rural Development) Rapp and Ely state that businesses are most susceptible to failure soon after organizing. The two provide a list of 10 actions cooperative organizers should follow to avoid common organizational pitfalls.

10 actions to avoid cooperative organizational pitfalls

1. Identify a clear mission for the cooperative with definite goals and objectives.
2. Create detailed plans for achieving the defined goals.
3. Make use of persons experienced in cooperative development.
4. Involve cooperative members or selected leaders in all decisions.
5. Develop board support among the potential member-users.
6. Hire experienced and qualified management.
7. Identify risks early in the organizational process.
8. Use realistic business assumptions.
9. Raise sufficient capital to survive the start-up period.
10. Keep the membership, suppliers and financiers informed.

Livestock slaughter and meat packing cooperatives are just as likely to fall prey to these pitfalls. Perhaps, given their competitiveness and slim operating margins, these industries are even more subject to these potential problems. Therefore, a lapse in only one area could leave the cooperative vulnerable and susceptible to failure. With this in mind, it is probably good to review the lessons learned since the first cooperative attempts to enter these industries 85 years ago.



Livestock producers in need of profits beyond the farmgate continue to eye co-op owned slaughter and meat packing operations as a primary option. USDA photo

Early livestock processing co-ops

The first recorded cooperative meat packing endeavor took place in La Crosse, Wis., in 1914. Twelve additional groups attempted to establish cooperative meat packing operations between 1914 and 1920. Of these efforts, only one lasted more than three years, and except for one, all ceased operations by 1923.

In 1957, when Fox looked back on these initial ventures, he saw some factors that contributed to their lack of commercial success. He summarized those he believed to be most critical in "Farmer Meat Packing Enterprises in the United States." A review of these factors shows they still have lessons to teach for those who plan to organize cooperatives today.

Fox found that the most common problem associated with cooperative meat packing efforts was lack of sufficient capital. He did not always attribute this to insufficient producer participation. Promoters were paid from 15- to 30-percent commissions on the capital they raised, which significantly reduced the net value of producers' investments.

Excessive valuation of existing facilities resulted in some cooperatives paying high prices for worn-out plants that required renovations, which further diluted the leverage of producer capital. In some cases, producers did not fully fund their stock subscriptions. Lack of producer support was exacerbated when farmers, ranchers and feeders became discouraged because immediate profits and dividends did not materialize as expected.

As with any business venture, capable management was an essential issue. Cooperatives often hired inexperienced and inefficient management, which manifested itself in overpayments for livestock, meat spoilage, inaccurate records, inability to collect accounts payable, extravagance, and lack of aggressiveness. These conditions further eroded producer support because producers lacked confidence in management.

Another area where these organizations had difficulties was their market position. In some cases, unsatisfactory sales outlets, keen competition and low prices also contributed to losses. Other projects were challenged by irregular and inadequate supplies of desirable livestock, or unfavorable freight rates for processed meat.

These conditions undermined the cooperative's ability to compete with established investor-owned firms. Because of these commercial failures, producer interest in cooperative livestock slaughter and meat packing remained dormant until 1930.

Meat Processing Co-ops, 1930-1948

Five of 13 slaughter and meat processing cooperatives started between 1930 and 1948 were still operating when Fox completed his analysis. Of the eight that failed, six operated for less than a year. Most of these failed attempts succumbed to the same factors that plagued earlier cooperative livestock slaughter and meat packing operations. Insufficient capitalization by producers, lack of producer commitment, inadequate marketing operations and inadequate management all contributed to their demise.

The factors identified by Fox have been corraborated by the experiences of later cooperative developers and researchers. The lessons from the commercial failures, coupled with those gained from commercially successful ventures, provide insight for people presently interested in organizing livestock slaughter or meat packing cooperatives. These lessons have been incorporated into the recommendations included in the 10 actions to follow during the developmental and planning process.

Unfortunately, not all the difficulties in cooperative organization remain in the distant past. Some recent organizational efforts did not result in commercial success. Several groups have repeated past mistakes. A review of some of these efforts shows the continued importance of careful planning before initiating operations.

Lamb co-op failures studied

Roland D. Smith and a team of others from Texas A&M University funded by USDA Rural Business-Cooperative Services completed a case study of produc-

er-owned lamb processing ventures started in 1989 and 1993. They found that lamb producers did a lot of things right in studying and preparing for the launching of the cooperatives. However, each business operated for less than two years.

Producers did many things right in launching lamb processing cooperatives, but old problems plagued the operations. *Photo courtesy American Sheep Industry Association Inc.*

Smith's team identified many of the same causes for failure that Fox had found more than 40 years earlier. The researchers categorized these factors into five areas: 1) inadequate financing; 2) limited management expertise; 3) misguided marketing efforts; 4) lack of consistent supply; and 5) the failure of the low-cost contract slaughter operation.

In describing lessons learned from the sheep experiences, the case study refers to planning as a critical element needed for success: "Had the contingency planning and effective evaluation been conducted as a proactive strategic process rather than as a reactive response to the existing economic environment, some of the perceived problems with financing, operations, marketing and management expertise would have been better addressed."

Indiana Family Farms, a pork cooperative, faced similar challenges. It initially purchased an old plant to renovate. But sufficient capital was not available. Probability of success was limited further by lack of producer support.

Indiana Family Farms estimated that 300 members were necessary for the project, while only 60 producers joined. It began custom slaughter, processing and distribution operations in November 1997. These operations were suspended in July 1998. In his column in "Feedstuffs," Steve Marberry concluded that "Buoyed by $60 per hundredweight hog markets [in 1996-97], producers decided to ride the spot market into an uncertain future."

Despite several unsuccessful efforts in organizing slaughter and processing cooperatives, a number are commercially successful. Farmland Industries entered the pork processing industry in 1959 by purchasing a plant. Today, Farmland is the fourth largest marketer of pork products in the United States and a leader in international value-added marketing.

In December 1997, U.S. Premium Beef initiated operations as a new-generation marketing cooperative. Operations began after 28 months of planning. Early

Interest in forming beef cooperatives remains high all across North America as producers seek higher profits and stability. *USDA Photo by Ken Hammond* this year, Chief Executive Officer Steven Hunt said the cooperative paid out more than $4.8 million in premiums over the cash live cattle market. This represents a $9 per head premium. During its first year of operation, the cooperative paid a total average return of 34 percent to its 675 members.

Producers continue to eye margins beyond the farm gate. Hog producers in North Carolina, Georgia, Illinois South Dakota and Minnesota; beef producers in plains and mountain states; as well as intermountain sheep producers are considering the potential for producer-owned, cooperatively governed slaughter and processing operations.

Prospering with co-ops

"Cooperatives are responding to the changes in one of the most aggressive restructuring periods in the history of American cooperation," says USDA's Torgerson. The current interest by producers to increase their share of the consumer's retail dollar through cooperatives offers them an opportunity to benefit from changing market processes. With care, producers can take advantage of these changes to prosper through cooperatives. Lessons learned from more than 85 years of cooperative slaughter and processing show how to avoid organizational pitfalls through planning. ■

Cooperatives' Response Needed for 1999 Survey

The annual survey of farmer cooperatives conducted by USDA's Rural Business-Cooperative Service (RBS) is the only source of detailed information on cooperatives and their service to American agriculture. This data source, the only one with a national scope, provides an important view of cooperatives' progress, growth and trends.

Data are collected annually to gauge current cooperative activities, develop trend lines, and obtain needed information for important research, education, and information on cooperatives.

How are the data collected?

The data are collected through the use of questionnaires. Similar questions are asked each year so that important data series can be maintained. Periodically, additional questions are included for conducting special studies of various aspects of farmer cooperatives. The 1999 survey will collect additional information for a special study of local cooperatives' involvement in providing crop protectants to their members.

Forms are mailed in early September to all cooperatives ending their business year between January and June. Cooperatives whose business year ends from July through September receive a questionnaire in early December. Those whose business year ends in the last quarter receive questionnaires in early March of the following year. Cooperatives are encouraged to furnish a copy of their annual or audit report along with the completed questionnaire. Such reports provide important information not requested on the questionnaire.

USDA/RBS staff maintain data for use in research, education and technical assistance. Any data used in presentations or publications are combined to maintain the confidentiality of individual cooperatives. Individual report forms are kept strictly confidential.

How are the data used?

Data collected from the annual survey of farmer cooperatives are combined, expanded to represent the total population, and selected data are published in reports such as: Rural Cooperatives, Statistical Abstract of the United States and Agricultural Statistics. Farmer cooperative statistics are used by cooperative leaders, educators, researchers, policymakers and others interested in farmer cooperatives. Agency staff frequently use the information for important studies and presentations. Educational materials, from pamphlets to college textbooks, rely heavily on statistics collected by the agency. Many people, including foreign visitors, contact the agency when they want to learn about the structure and operation of U.S. farmer cooperatives.

How can farmer cooperative statistics be acquired?

A copy of the annual statistics report is sent to each cooperative. Additional copies of the report can be ordered from RBS. If you have questions regarding farmer cooperative statistics, please call, e-mail or write Charles A. Kraenzle at (202) 720-3189, or charles.kraenzle@usda.gov, or USDA/RBS/Statistics, STOP 3256, 1400 Independence Ave, SW, Washington, DC, 20250-3256.