

## Chapter 3. Cooperatives

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Farmer cooperative sales throughout the United States and New York State set new records in 2011, which demonstrates the vitality of the nation's farmer-owned cooperatives and the important role they play in the agricultural sector. Total net business volume of cooperative businesses (excludes sales between cooperatives) grew by 24 percent nationally and 22 percent in New York State. Noteworthy research has been conducted over the past several decades to document the importance of cooperative businesses. Similar to investor-owned firms, cooperatives must adapt to a variety of external and financial factors in order to remain profitable and add value to the businesses of their producer members. The following chapter provides an overview of cooperative activity within the United States and New York State and provides insight into the critical issues facing cooperatives in the future.

### U.S. Situation – Farmer Cooperatives

In 2011, 2,285 U.S. farmer cooperatives owned by 2.3 million members had a record-breaking year with over \$213 billion in gross business volume (includes sales between cooperatives) and nearly \$613 million returned to member owners in patronage refunds (Table 3-1). Higher commodity prices in 2011 resulted in farmer cooperatives nationwide (excluding the Farm Credit System) increasing gross business volume by 11 percent from the previous record high of \$191.9 billion set in 2008. This is also a \$41.3 billion increase, or 25 percent over 2010. Table 3-1 compares volume of cooperative business between 2010 and 2011.

Item	2010 (\$ billion)	2011 (\$ billion)	Change percent
<b>Gross Business Volume</b>			
Marketing	\$101.1	\$128.1	26.7%
Farm Supplies	63.9	80.9	26.8
Services	5.0	4.5	-10.0
<b>Total</b>	<b>\$170.1</b>	<b>\$213.4</b>	<b>25.4%</b>
<b>Balance sheet</b>			
Assets	\$65.0	\$78.5	20.8%
Liabilities	39.0	50.6	29.7
Equity	26.0	27.9	7.3
<b>Income Statement</b>			
Sales (Gross)	\$171.8	\$213.4	24.3%
Patronage income	0.7	0.6	-11.4
Net income before taxes	4.3	5.4	25.6
<b>Employees</b>			
	(Thousand)	(Thousand)	
Full-time	129.0	130.9	1.5%
Part-time, seasonal	54.4	52.8	-2.8
<b>Total</b>	<b>183.4</b>	<b>183.7</b>	<b>0.2%</b>
<b>Membership</b>			
	(Million)	(Million)	
	2.2	2.3	4.5%
<b>Cooperatives</b>			
	(Number)	(Number)	
	2,314	2,285	-1.3%
Source: Cooperative Statistics 2011, USDA Office of Rural Development <a href="http://www.rurdev.usda.gov/BCP_Coop_DirectoryAndData.html">http://www.rurdev.usda.gov/BCP_Coop_DirectoryAndData.html</a>			

While not shown, net business volume (excludes sales between cooperatives) grew by 24 percent or \$35.8 billion from \$147.8 billion in 2010 to \$183.6 billion in 2011. Most of this (82%) can be attributed to increasing dairy and grain and oilseed prices, with dairy product marketing cooperative volume increasing by \$8 billion and grain and oilseeds marketing cooperative volume increasing by \$13.4 billion. Net business volume for supply cooperatives increased \$10.2 billion, with increasing prices paid for feed, fertilizer, and petroleum accounting for 87% of the increase. Net business volume increased \$1.9 billion, \$2.3 billion, and \$3.6 billion for feed, fertilizer, and petroleum products, respectively.

The aggregate cooperative balance sheet shows total assets increased by \$13.5 billion or 21 percent and liabilities increased by \$11.6 billion or 30 percent between 2010 and 2011. Equity improved by \$1.9 billion or slightly over 7%. Net income before taxes increased \$1.1 billion or 25.6 percent between 2010 and 2011.

Nationally, farmer marketing cooperatives account for 53.5 percent of all farmer cooperatives with 36.6 percent of all memberships. Supply cooperatives account for 40.9 percent of all U.S. farmer cooperatives and 61.7 percent of all memberships. Farmer service cooperatives make up the balance; i.e. 5.6 percent of cooperatives with 1.7 percent of memberships. Membership numbers exceed farm numbers as a farm business can belong to one or more cooperative enterprises. The total number of cooperatives declined modestly between 2010 and 2011 (-1.3 percent), reflective of continued industry consolidation (Table 3-1). While farmer cooperative members have also trended downward over the last decade, total memberships increased modestly between 2010 and 2011 by 4.5 percent. This result was largely influenced by strong growth in the number of grain and oilseed cooperative memberships (+159,000) that more than offset relatively sizable declines in memberships for tobacco marketing cooperatives (-53,000) and supply cooperatives in total (-64,100).

The number of full- and part-time workers remained relatively constant in 2011 at 183.7 thousand workers, with a modest increase (1.5 percent) in full-time workers to 130.9 thousand (Table 3-1). Notably, full-time employment is up over 7 percent from its five-year low in 2009. Marketing cooperatives employ 57 percent of the farmer cooperative labor force, followed by supply cooperatives at 42 percent, and service cooperatives at 1 percent. Grain and oilseed marketing cooperatives employed 24,300 employees, with an increase of 8 percent from 2010 to 2011. Likewise, dairy cooperatives employed 20,800 employees in 2011, with an increase of 10 percent over 2010. Fruit and vegetable marketing cooperatives employed 13,500 employees in 2011, with an increase of 1.5 percent over 2010. These three sectors employ approximately 45 percent of all farmer cooperative workers.

### **New York State Situation**

Data for agricultural cooperatives headquartered in New York State were obtained through a USDA Rural Development Cooperative Service survey. The most current state-level information available is for years 2010 and 2011. Table 3-2 summarizes cooperative businesses headquartered in New York State.

Between 2010 and 2011 the total number of farmer cooperatives (55) and cooperative memberships (6.4 thousand) were stable. The number of dairy cooperatives and the number of fruit and vegetable cooperatives decreased by one in each category, while the number of “other product” marketing cooperatives increased by two. Dairy and fruit and vegetable cooperatives maintained membership as cooperatives are more likely to merge rather than disband. Two “other products” marketing cooperatives reported to the survey increasing membership by 100.

Reflective of improved milk prices in 2011, net business volume for dairy cooperatives increased by nearly \$405 million or 23 percent from 2010 levels. New York State dairy cooperatives market approximately 75 percent of the milk produced within the state. Fruit and vegetable and other products

<b>TABLE 3-2. NEW YORK STATE AGRICULTURAL COOPERATIVE NUMBERS, MEMBERSHIPS AND NET BUSINESS VOLUME, 2010 and 2011<sup>1</sup></b>						
<b>Major Business Activity</b>	<b>Number &amp; Membership (000) Headquartered in State</b>				<b>Net Business Volume</b>	
	<b>2010</b>		<b>2011</b>		<b>2010</b>	<b>2011</b>
	No.	Members (000)	No.	Members (000)	(\$ million)	
<b>Marketing:</b>						
Dairy	31	3.5	30	3.5	\$1,738.5	\$2,143.4
Fruit & Vegetable	9	1.0	8	1.0	70.5	74.8
Other Products <sup>2</sup>	3	0.2	5	0.3	170.8	184.8
<b>TOTAL MARKETING</b>	<b>43</b>	<b>4.7</b>	<b>43</b>	<b>4.8</b>	<b>\$1,979.7</b>	<b>\$2,403.0</b>
<b>Supply:</b>						
Crop Protectants					\$13.2	\$22.9
Feed					71.6	74.3
Fertilizer					18.1	31.4
Petroleum					2.5	2.3
Seed					2.7	3.6
Other Supplies					19.5	27.5
<b>TOTAL SUPPLY</b>	<b>6</b>	<b>1.4</b>	<b>6</b>	<b>1.4</b>	<b>\$127.7</b>	<b>\$162.0</b>
<b>TOTAL SERVICE<sup>3</sup></b>	<b>6</b>	<b>0.3</b>	<b>6</b>	<b>0.2</b>	<b>\$15.5</b>	<b>\$31.5</b>
<b>TOTAL</b>	<b>55</b>	<b>6.4</b>	<b>55</b>	<b>6.4</b>	<b>\$2,123.0</b>	<b>\$2,596.6</b>

Source: *Cooperative Statistics* 2011, USDA Rural Development, [http://www.rurdev.usda.gov/BCP\\_Coop\\_DirectoryAndData.html](http://www.rurdev.usda.gov/BCP_Coop_DirectoryAndData.html)

<sup>1</sup> Totals may not add due to rounding.

<sup>2</sup> Includes wool, poultry, dry bean, grains, livestock, maple syrup, ethanol, and miscellaneous cooperatives.

<sup>3</sup> Includes those cooperatives that provide services related to cooperative marketing and purchasing.

cooperatives increased volumes by 6 percent and 8 percent, respectively, and resulted in net business volume for all reporting marketing cooperatives to increase by \$423.3 million or 21 percent.

The database indicates that there are six farmer supply cooperatives and six farmer service cooperatives in New York State. Producers experienced higher costs for inputs in 2011 and these higher costs are reflected in higher business volumes for crop and livestock inputs in supply cooperatives. Net business volume from seed sales increased 30 percent and net business volumes from crop protectants and fertilizer increased by over 70 percent each. In total, net business volume for supply cooperatives increased by \$34.4 million, or 26.9 percent. The robust increase in farmer cooperative services resulted in net business volume doubling from \$15.5 million to \$31.5 million. Overall, net business volume for those cooperatives headquartered in New York State increased by \$473.6 million or 22 percent.

The USDA Rural Development Cooperative Survey does not include activity of the Farm Credit System. According to the 2011 Farm Credit East Annual Report, on January 1, 2010 Farm Credit of Western New York, ACA merged into First Pioneer Farm Credit, ACA to create Farm Credit East, ACA. Farm Credit East, ACA service area includes New York State, New Jersey, Massachusetts, Connecticut, Rhode Island, New Hampshire, and customers in several other states. As such there are no figures specific to New York State; however 52 percent of the loan portfolio is based in New York State. The 2011 Farm Credit East ACA annual report notes that loan volume increased slightly less than 2 percent from \$4.3 billion to \$4.4 billion. Net income before taxes rose from \$134.43 million to \$141.40 million. The board of directors determined that \$35.5 million be returned in cash refunds, the cooperative's 16<sup>th</sup> consecutive patronage distribution.

### Issues for Agricultural Cooperatives

In 2011, the Council on Food, Agriculture, and Resource Economics (C-FARE) convened a panel of 24 cooperative CEOs, USDA researchers, and academic specialists to learn more about critical issues facing today's cooperatives. Cooperative businesses are different from other types of investor owned firms in that they are owned by member patrons who have democratic control with a portion of the net revenues returned to members through patronage refunds. Panelists were asked to rate a series of issues as extremely important, very important, important, somewhat important, and not important. The issues were grouped as shown in Figure 3-1.:

<b>FIGURE 3-1. CRITICAL ISSUES FACING COOPERATIVES, C-FARE PANEL, 2011</b>		
Issue	Sub-issues	
External	<ul style="list-style-type: none"> <li>• Industrial competition</li> <li>• Market concentration</li> <li>• Public policy</li> <li>• Regulation</li> </ul>	<ul style="list-style-type: none"> <li>• Global competition</li> <li>• Consumer preferences</li> <li>• Market volatility</li> </ul>
Finance	<ul style="list-style-type: none"> <li>• Tax issues</li> <li>• Outside equity</li> <li>• Unallocated equity</li> <li>• Risk management</li> </ul>	<ul style="list-style-type: none"> <li>• Profitability</li> <li>• Financial competency</li> <li>• Adequate equity</li> </ul>
Strategy	<ul style="list-style-type: none"> <li>• Decision making</li> <li>• Aligning incentives</li> <li>• Cooperation with cooperatives</li> </ul>	<ul style="list-style-type: none"> <li>• Efficiency</li> <li>• Succession</li> <li>• Human resources</li> <li>• Planning</li> </ul>
Governance	<ul style="list-style-type: none"> <li>• Balancing cooperative and member needs</li> <li>• Board dedication</li> <li>• Board competency</li> </ul>	<ul style="list-style-type: none"> <li>• Member involvement</li> <li>• Board operations</li> <li>• Board orientation</li> <li>• Recruiting board members</li> </ul>
Communication	<ul style="list-style-type: none"> <li>• Public understanding</li> <li>• Educating youth</li> </ul>	<ul style="list-style-type: none"> <li>• Educating members</li> <li>• Value to members</li> </ul>

Source: Kenkel and Park, 2011.

The following is a brief summary of the panel results.

**EXTERNAL:** Market volatility and public policy were deemed extremely important to very important by 80 percent of participants. Over 60 percent identified industry competition, market concentration and global competition as extremely important or very important. Nearly one-third of the panel viewed consumer preferences as extremely important.

**FINANCE:** Financial issues are one way to examine factors internal to the cooperative business. Profitability was rated extremely to very important by all respondents. In addition, 90 percent of respondents indicated that adequate equity and financial competency was extremely important or very important. The cooperative profit stream is used to build equity for the cooperative businesses while simultaneously returning patronage and retiring equity of member owners. The most critical challenge identified was the need to acquire and maintain equity accounts that would finance growth and provide working capital when necessary. The second financial challenge identified was the need for adequate profitability to finance the assets and strengthen the balance sheet. Most equity capital is derived from earnings. The third most mentioned challenge was balancing the tradeoff of the proportion of equity investment on the part of the member with the need of the cooperative to retain more equity as a risk management tool.

**STRATEGY:** External and financial issues can be addressed and managed through competent people with the ability to create and implement a strategic plan that positions the cooperative for growth and returns to members and patrons. Almost 90 percent of the panel indicated that a sound strategic plan was important to extremely important. Over 90 percent of the panel indicated that human resources were critical to the success of the cooperative enterprise. More specifically, "...[T]he succession of management and key personnel, attracting and maintaining high quality personnel, and aligning the incentives of managers and employees with member interests all received high importance ratings." (Kenkel and Park, 2011).

**GOVERNANCE AND COMMUNICATION:** Competent employees and management is critical to the success of a cooperative business. At the same time there is a need for competent cooperative board. Eighty percent of the panelists suggested that recruiting board members with the necessary critical thinking skills and decision making capabilities is extremely important, with the remaining 20 percent indicating that this is very important. Board members are the linkage representing the interests of the members when making decisions regarding cooperative policies and goals. The directors are charged with rationalizing business decisions to members that ultimately impact equity funds retained in the cooperative business and profits distributed patrons. Over 60 percent of the panel indicated that communicating the value of the cooperative business to its members was extremely important, with another 30 percent indicating that it was very important.

### **Cooperative Outlook for New York**

Through a resolution passed by the United Nations, 2012 was designated the International Year of the Cooperative. The International Cooperative Alliance found that the combined economic activity of the top 300 cooperatives in the world would create the 9<sup>th</sup> largest economy (World Cooperative Monitor). Nine of the top fifty-one dairy cooperatives within the United States have members in New York State and of those nine, five are headquartered in New York State (Hoard Dairyman 2012). Cooperatives play a significant role in the farm and food sector in the state.

The initial high temperatures and subsequent freezing temperatures experienced by fruit growers in early spring decreased fruit yields significantly. Decreased fruit yields will likely impact the financial statements of fruit cooperatives over the next two years. Drought conditions of 2012 have reduced the roughage available to dairy farms. Some farmers were able to harvest additional cuttings and others double cropped small grain acreage as a means to close the gap of forage demands of dairy cattle. Drought experienced throughout the Midwestern part of the United States increased price levels and volatility in grain markets. As a result, one of the biggest challenges facing dairy farmers is the volatility in grain markets and subsequent input costs coupled with a decreasing milk price. Cooperative leaders and farmers have voiced concerns over the lack of passage of the Farm Bill and the impending "fiscal cliff" with the potential negative impact on the economy and consumer purchasing patterns.

Dairy cooperatives have voiced concern over expanding milk supply to meet the increasing need for product for yogurt production. Cooperatives partition the milk produced by member farms to existing and potential customers. Class I milk sales are preferred because of the higher prices received compared to Class II, III, or IV. In spite of transportation costs, shipping milk from the Northeastern United States to the Class I deficit areas of the Southeastern United States can result in higher average milk prices received by dairy farmers, even though there is increased local demand for Class II milk for yogurt production. The reality is that dairy cooperatives do not increase the supply of milk in the market. Growth decisions are made by individual farm businesses. "Each owner makes this decision on the basis of their business, and often the family's goals and the opportunities that they see before them. Growth may be an industry goal, but it is a firm decision." (Novakovic, 2012).

Profitability is key for any business to remain viable into the future. Profitability within a business is influenced by internal controls responding to external conditions. Cooperatives have and will continue to

investigate opportunities to build joint ventures that leverage resources, minimize risk, and build profitability. Unique to the cooperative business model is to return patronage income to their members and, as such, the cooperative becomes an extension of and adds value to the members business. Several boards of directors and management are actively engaging in the strategic planning process to chart a course of action that embraces both the challenges and opportunities for the cooperative business to align with the goals of the membership.

Although 2012 brought a number of trials to cooperatives and their farmer members operating in New York State, these farmer-owned businesses will remain well positioned for solid performance in 2013.

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