

Is Equity Actually Debt? The Curious Case of Cooperative Finance

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Our purpose is to determine, develop and deliver research and education for the cooperative community.



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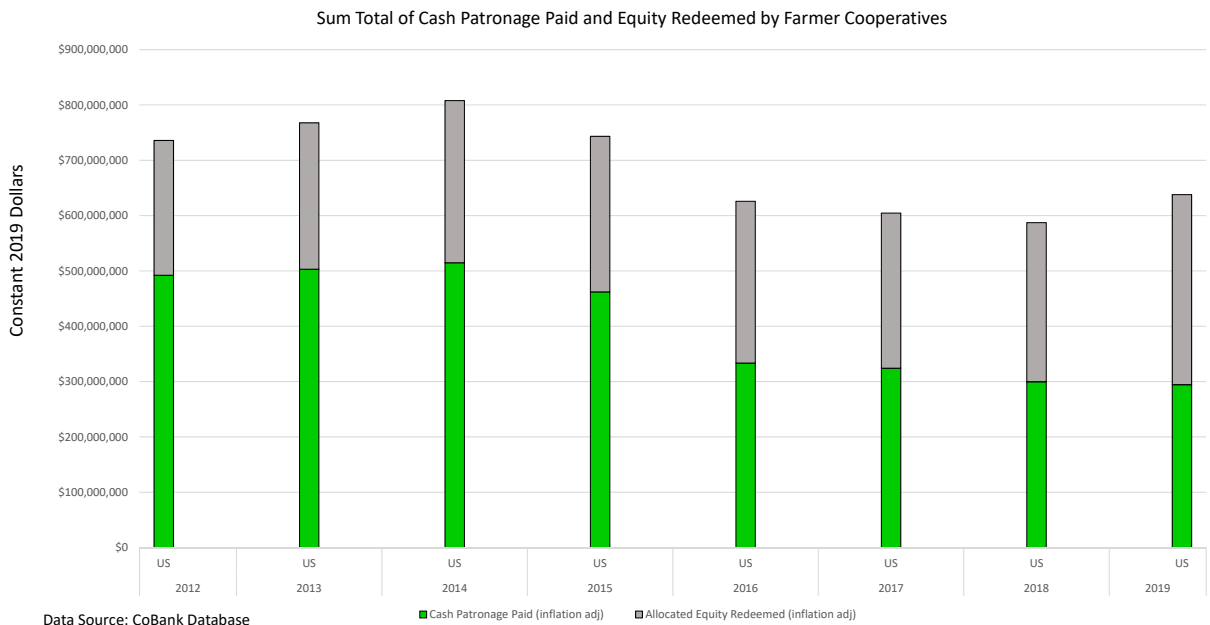
The importance of cooperative profits

- Without profits, how do you service or meet the needs of your farmer-owners?
- Used to capitalize the business (equity) and distributed proportionally on the basis of use



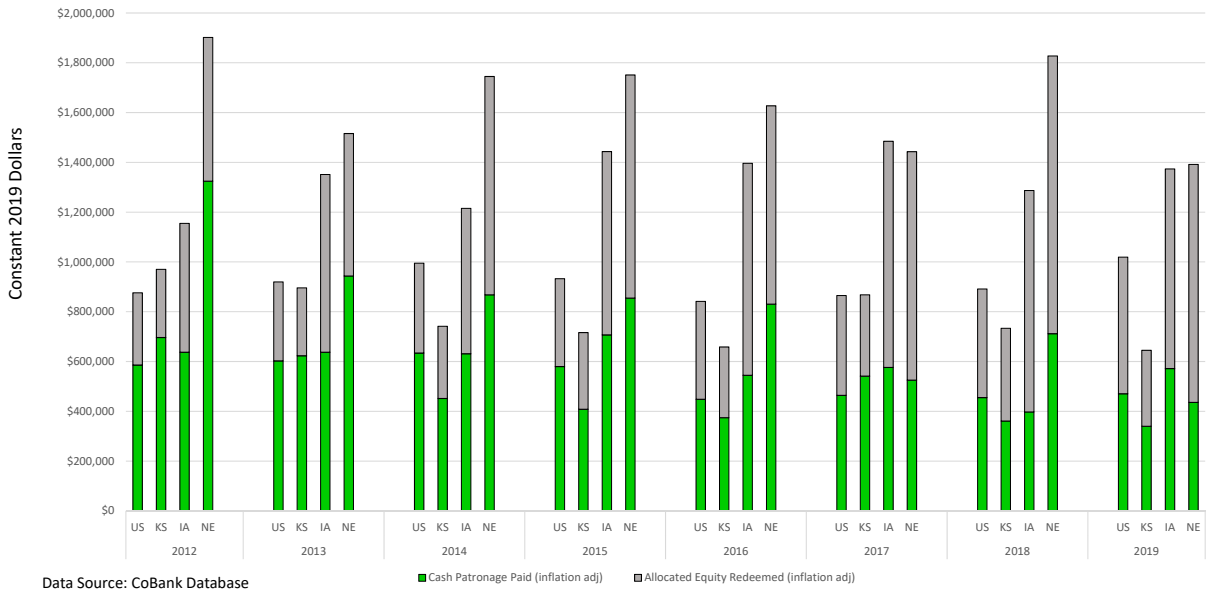
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Total cash and equity paid is quite sizable and follows the agricultural cycle



Paying cash patronage and redeeming equity has an impact on farmer-patrons but also on growth

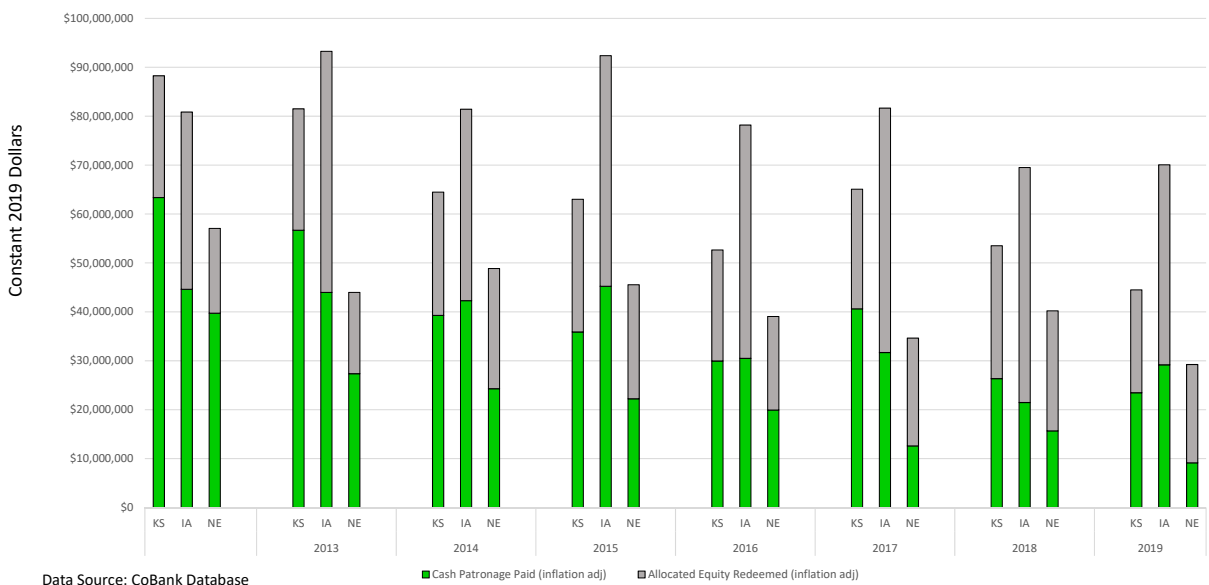
Average Cash Patronage Paid and Equity Redeemed by Farmer Cooperatives



Data Source: CoBank Database

Total cash and equity paid is quite sizable

Sum Total of Cash Patronage Paid and Equity Redeemed by Farmer Cooperatives



Data Source: CoBank Database

Cooperative

Balance Sheet	
Assets	Debt
Current	Current
	Non-current
	Equity
Non-current	Unallocated (Retained Earnings)
	Allocated (Retained Patronage)
	Stock

Investor Owned Firm

Balance Sheet	
Assets	Debt
Current	Current
	Non-current
	Equity
Non-current	Retained Earnings
	Stock

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How is allocated equity redeemed?

1. Special situation plan (estates, no longer farming, no longer a member, etc.)
2. Age of patron (patron turns a certain age, receives their allocated equity)
3. Percentage-of-all-equities (redeem a flat percentage)
4. Revolving fund (allocated equity turns a certain age, paid back to patron)
5. Base capital (complicated...want to know more? Take my AGECE 470 Co-ops class!!!)

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Some states require equity redemption

- Prior to the 1970s, cooperatives rarely redeemed equity
- In response, the following states passed legislation requiring cooperatives to redeem equity upon death
 - Iowa
 - Nebraska
 - New Mexico
 - Rhode Island
 - South Carolina
- Do cooperatives in these states manage equity differently?

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Cooperative

Balance Sheet	
Assets	Debt
	Equity
Current	Current
	Non-current
	Allocated (Retained Patronage)
	Unallocated (Retained Earnings)
Non-current	Stock

Investor Owned Firm

Balance Sheet	
Assets	Debt
	Equity
Current	Current
	Non-current
	Retained Earnings
Non-current	Stock



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Regression results – Correlation with future profitability?

- CoBank panel data that spans 1996 to 2014 with 155 grain and farm supply co-ops
- ROE = lagged (CR, AE, ROE, NPM, ATR, INT, SD_ROE, TOTassets, Net New Equity, Net New Equity_Interact)
- Significant positive results (correlated higher future ROE)
 - AE, ROE, NPM, Net New Equity
- Significant negative results (correlated lower future ROE)
 - CR, Net New Equity_Interact

Conclusion and implications

- Cooperative equity capital challenge
- Redeeming equity versus stock buyback
 - What are your reasons?
- Cooperatives that add “net” new allocated equity tend to have higher future profitability
 - Not retiring too much equity
- Iowa and Nebraska cooperatives are the opposite...more “net” new allocated equity tend to have lower profitability
- Be mindful of retiring equity

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Thank you

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