

Sustainable Growth Rates of Farmer Cooperatives: Who is Growing Broke?

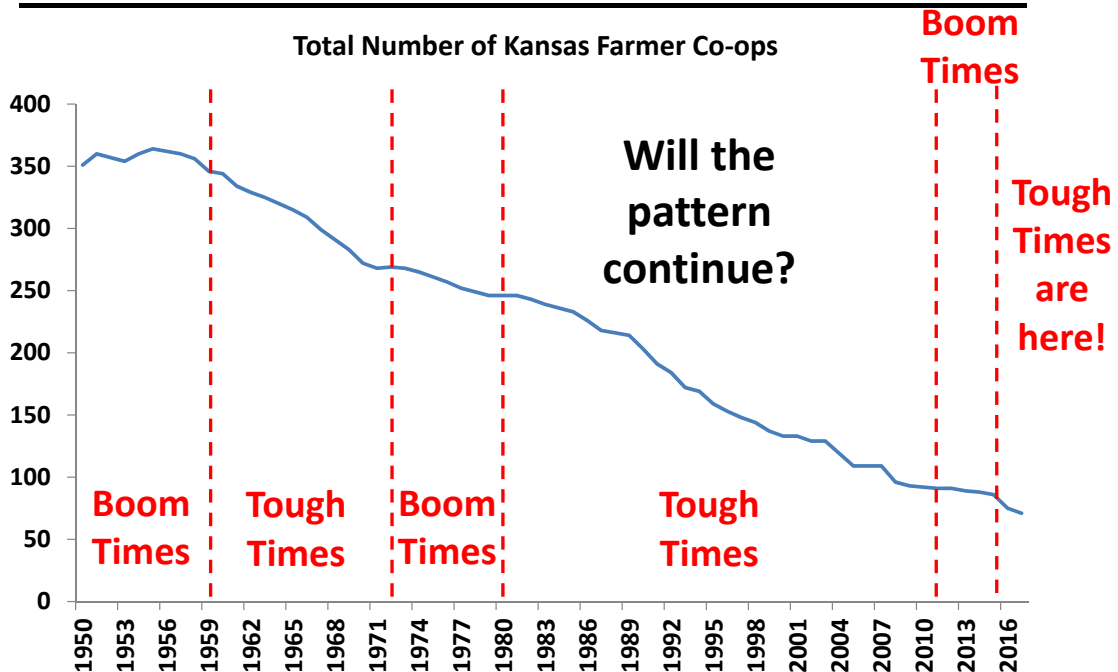
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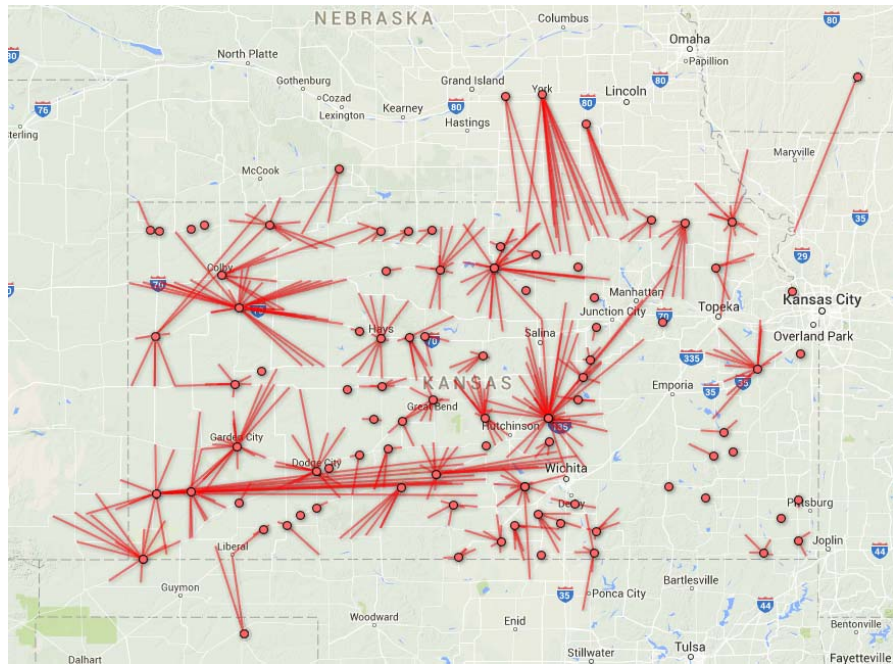


Total number of Kansas farmer co-ops has fallen and the pace of decline might accelerate.

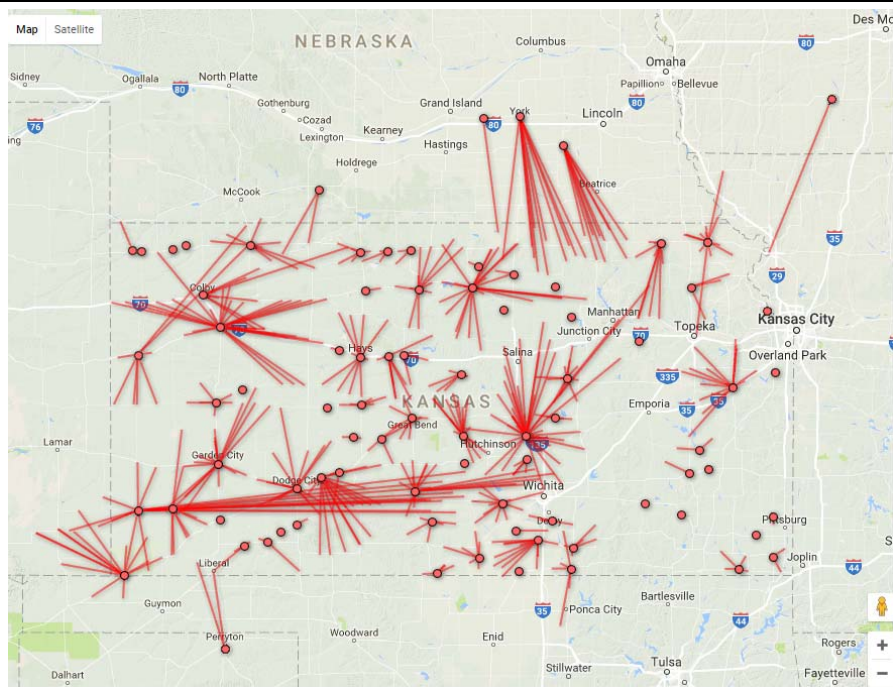


Source: USDA NASS and ACCC

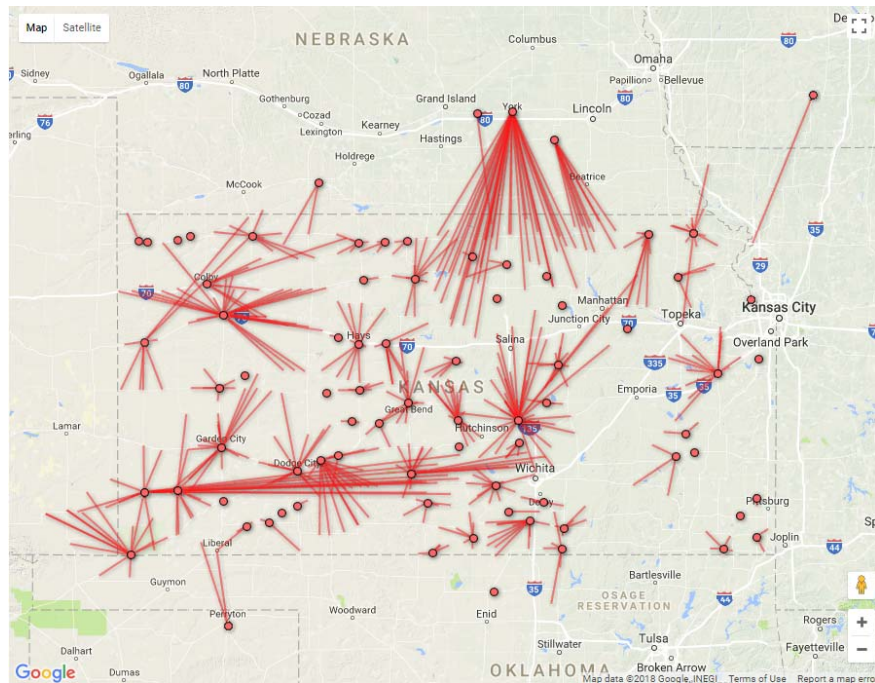
81 farmer co-ops with a Kansas HQ January 2016



76 farmer co-ops with a Kansas HQ January 2017



71 farmer co-ops with a Kansas HQ January 2018



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Where are we heading in Kansas? Fewer co-ops?
Yes. But how many? 50? 40? 20?

- Retiring managers
- LLC formation...death to mergers?
 - Why does this happen in Kansas and hardly anywhere else?
- Farmer-owners are changing
 - Fewer of them
 - More efficient
 - Bigger
 - Today, financially stressed?

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Sustainable Growth Rates

- Lots of discussion of growth and the need to grow
- Not as much discussion of, are we growing too fast or too quickly?
- Could the concept of a “sustainable growth rate” help grain marketing and farm supply co-ops make more informed decisions about growth?

What is a sustainable growth rate?

- A sustainable growth rate is the rate at which a company can grow without having to borrow money to fund its growth.
 - Using internal controls to fund that growth
- Higgins (2007) presents a straightforward model for co-ops:

$$SGR = \left(1 - \frac{Cash\ Pat}{NI}\right) \left(1 + \frac{Debt}{Equity}\right) \left(\frac{NI}{Sales}\right) \left(\frac{Sales}{Assets}\right)$$

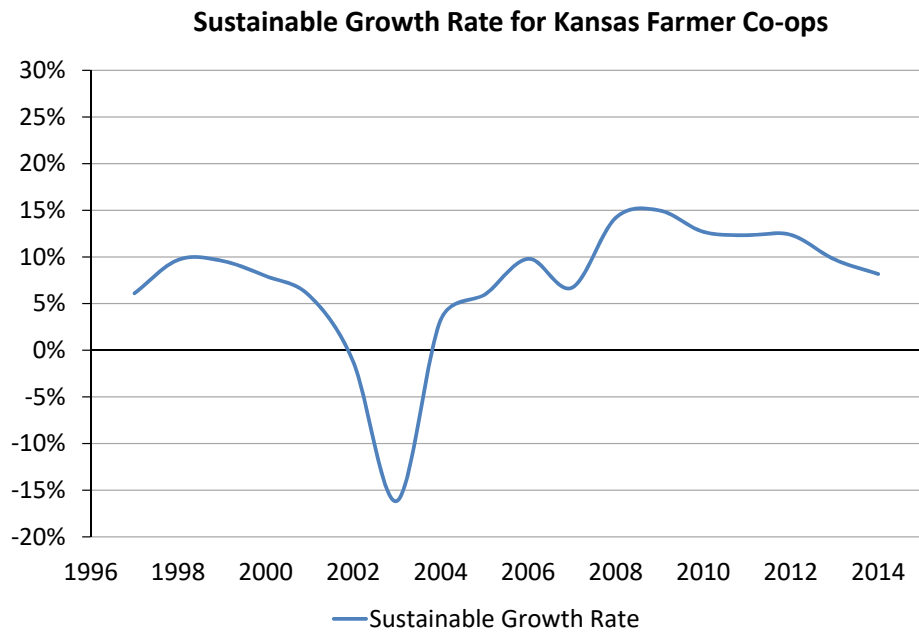
Earnings
Retention

Leverage

Profit
Margin

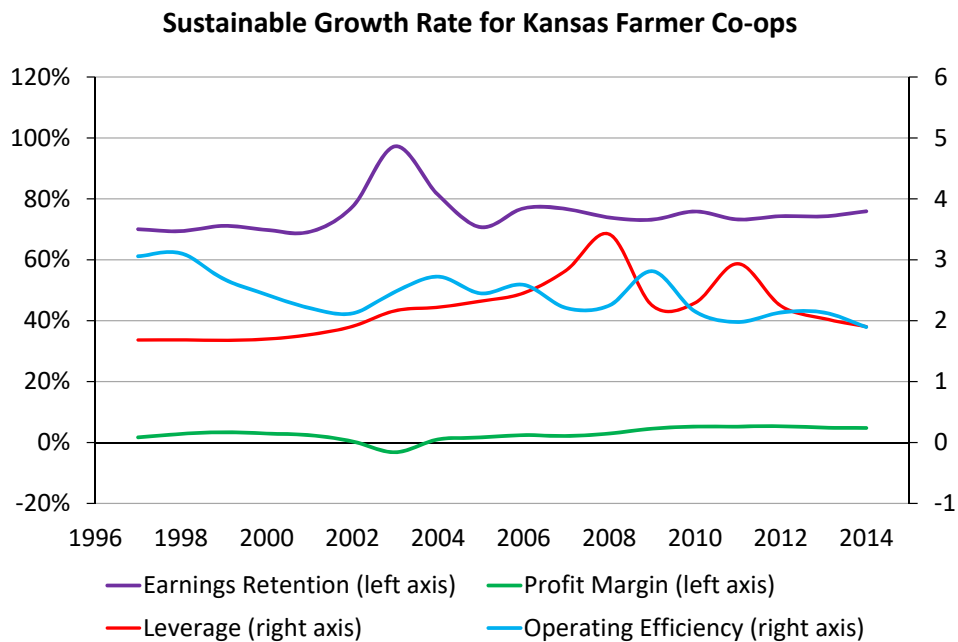
Operating
Efficiency

Sustainable growth rates accelerated during the boom and are coming back down.



Source: CoBank RiskAnalyst Data

Sustainable growth is driven by four key components.



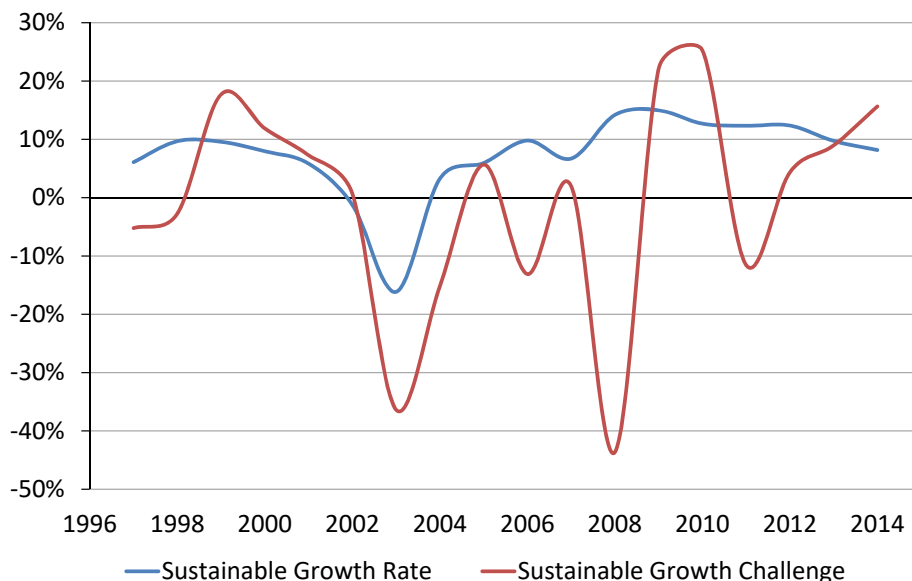
Source: CoBank RiskAnalyst Data

How do sustainable growth rates vary across cooperatives?

- Small cooperatives (<\$50 million in sales) SGR is about 3 percent lower than larger cooperatives (>\$50 million in sales)
 - Not much differentiation in SGRs in the “larger” group
- Cooperatives located in the Corn Belt have a 1 percent larger SGR than non-Corn Belt cooperatives
- Cooperatives with a majority of farm supply sales have a 1 percent lower SGR than cooperatives with a majority of sales coming from grain

At times, actual growth outpaces sustainable growth creating a challenge...then what?

Sustainable Growth Rate and Challenge for Kansas Farmer Co-ops



Source: CoBank RiskAnalyst Data

How do cooperatives overcome growth challenges?

- Estimated a seemingly unrelated regression model to control for endogenous regressors
- The decision to address a sustainable growth challenge (SGC) involves 'levers' that are related
- So, what type of co-op uses what type of 'lever'?

How do cooperatives overcome growth challenges?

- Leverage is very important for all cooperatives
- Profit margin is not beneficial to address a SGC
- These types of cooperatives rely more on leverage and operating efficiency than their associated counterpart:
 - Small (<\$50 million in sales) relative to large
 - Corn Belt relative to non-Corn Belt
 - Majority Farm Supply Sales relative to Majority Grain Sales

So, who is growing broke?

- Those cooperatives who are not investing for future growth
 - Distributing large cash patronage payments
 - Low operational efficiency
- Cooperatives do not appear to have a sustained and persistent growth challenge
 - Profitable, efficient, and have a good relationship with a lender
- Important for board of directors to have a balanced approach to distributing patronage and reinvesting for the future

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Thank you

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