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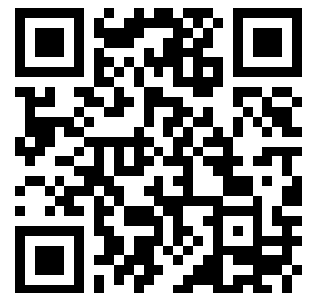
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Local and Regional Cooperative Relationships in Two Federated Systems

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Abstract

Local and Regional Cooperative Relationships In Two Federated Systems

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An analysis of operations of 18 member locals and two Midwestern regional cooperatives shows that local use of regionals, management practices, and cooperative competition can affect operating relationships of local and regional cooperatives. Findings in this report are based on a series of personal interviews with regional managers and managers of nine member locals of each regional. Information contained in the report reflects cooperative organization and structure, business and financial operations, management policies and practices, cooperative and other competition, and cooperative services to farmers. The focus of efforts in the two systems was found to be in ways to improve overall system efficiency and control.

Key words: Cooperatives, locals, regionals, competition, management practices, federated systems.

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Preface

This study is the second of two studies about the nature of the relationships between local and regional cooperatives in a federated system. Findings in this report are based on a series of personal interviews with regional managers and managers of nine member locals of each regional. An analysis of the operations of 18 member locals and two Midwestern regional cooperatives was undertaken to assess the effect of various factors on the operating relationships of local and regional cooperatives. The factors considered were cooperative organization and structure, business and financial operations, size, management policies and practices, cooperative and other competition, and cooperative services to farmers.

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Highlights

In their relations with local cooperatives, regionals now tend to focus more on providing advisory and support services and less on carrying out their traditional distribution functions. The presence or absence of intercooperative competition at the regional level is a contributing factor to the changing nature of the relationship between regionals and locals.

Taken together, the locals experienced declines in dollar volumes in both supplies and grain marketing. Total sales of 18 local cooperatives averaged \$15.6 million in 1985, down 5 percent from \$16.5 million in 1981. Supply sales were off 4 percent, and marketing sales fell 7 percent between 1981 and 1985. The leading product sold in both regions was petroleum, followed by fertilizer. Average product sales were down 2 percent in region A and 5 percent in region B from 1981 to 1985.

Total assets and liabilities declined between 1981 and 1985 for the average local in regions A and B. Net worth of the average local in region A increased by 13 percent and in region B by 2 percent. Net savings fell about 20 percent due to decreased refunds from regionals. Operating margins at the local level held fairly steady.

In region A, locals encounter a considerably higher degree of competition from other cooperatives in all supply groups. In addition, several regional cooperatives were competing for the retail business of locals, duplicating services and increasing costs to farmers. In region B, competition among cooperatives is limited to fringe areas of trade territories.

The 18 locals involved in the study had an average of 32 percent of the share of the farm supply market within their trade territory. On an average, the larger locals were able to obtain larger shares of the various supplies than the smaller locals.

Managers felt that the major weaknesses in their organizations were internal management, communications, and decisionmaking practices. They believe cooperative members must begin to pay only for services they receive.

Locals in regions A and B purchased 80 and 83 percent, respectively, of their total supplies from their regional cooperatives. Noncooperative suppliers accounted for 14 and 15 percent of total supplies purchased.

About 41 percent of products purchased by locals in region A were delivered by the regional, 27 percent by locals, and 32 percent by contract haulers or others. Small and medium locals in region A were more dependent on the regional for delivery of their products than were large locals. Locals in region B were less dependent on their regional for delivering supplies averaging 12 percent.

The division of responsibility for providing functions and services between the locals and regionals was essentially the same for the two regions. Services such as farm management analysis, seed and soil testing, and chemical and pesticide recommendations were generally provided by the regional.

Locals in region A included service costs in product prices in 67 percent of services and added extra charges for 33 percent of services. Locals in region B included cost in price in 57 percent of services and added extra charges for 43 percent of services provided farmers. The greater degree of intercooperative competition in region A may have the effect of slowing actions to establish separate charges for services.

Local managers expressed strong confidence in the ability of their regional to serve member locals. By a 2-to-1 margin, local managers thought regionals should get more involved in local management, while the minority thought the level of involvement should stay about the same.

Ratings by local managers indicated the highest level of regional involvement in local operations was in the areas of product sales, personnel training, and product information. The lowest level of regional involvement was in credit policy, personnel selection, and operating efficiency. Ratings of involvement were quite consistent among all cooperatives.

Regional managers indicated several factors or conditions which lead to increased involvement by their regional. These include small size, poor financial condition, weak managers, and a weak local board of directors. Regional involvement has increased in the last 5 years, according to regional managers, and they expect this trend to continue.

Local managers indicated the highest level of involvement was in training specialists, field personnel, and information specialists. The lowest level of involvement was with regional board members, telecommunications specialists, and division heads.

Larger locals indicated a relatively lower level of involvement by regional field personnel, likely a result of locals having a greater level of product expertise represented on their own staffs. On the other hand, the greater complexity of managing larger local cooperatives has led, apparently, to a relatively higher level of involvement by regional management specialists in large local operations.

The federated regionals in the study have moved in different directions to adjust to changing conditions. Regional A undertook joint efforts with other cooperatives. Regional B adopted a strict membership agreement designed to increase the flow of goods and services within their cooperative system.

In federated systems, a close working relationship between the regional and local provides coordinated operations required to fulfill farmers' needs. They are successful when management of the regionals is committed to serving member locals in ways that benefit farmers. Emphasis on local achievement through regional involvement is a key to a successful system.

Local and Regional Cooperative Relationships in Two Federated Systems

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This study examines the relationship between local and regional cooperatives in two federated cooperative systems. The two regional organizations are designated regional A and regional B in this report. Regional A has sales of more than \$1.0 billion per year, primarily in farm supplies, spread over a multistate area. Regional B also has sales of over \$1.0 billion, slightly more than half in grain marketing, and operates in a more geographically focused trade territory.

As farmers and farming operations have changed, so has the operations of local cooperatives serving those farmers. Both regional organizations have seen the effects of these changes on the type of services and products they provide for their member locals. While the physical handling of "hard" products, including warehousing, holding inventory, and transporting, remains important, increasingly regionals are providing "soft" services for their locals. Examples of these include education and training programs; technical and management consulting; financial recordkeeping and consulting; computer software, timeshare, and use assistance; and communications. Increasingly, the traditional distribution functions of the regionals are becoming relatively less important as more products are being shipped directly to locals, picked up by locals, or moved to locals by contract haulers.

While both regional systems exhibit similarities across a number of dimensions, one major difference must be noted. In the area served by regional A, a number of other regional cooperative systems are also operating. In contrast, regional B operates in an environment of a single regional system competing only with proprietary firms.

STRUCTURE AND OPERATIONS OF LOCAL COOPERATIVES

Local cooperatives involved in this study may be both compared and contrasted on the basis of structure, operations, and intercooperative competition. Local cooperatives in the two systems have many similarities, but they also have a number of quite significant differences. The relationship between the locals and regionals in the two systems, as well as the way locals do business, is affected by the presence or absence of intercooperative competition at the regional level.

Regional cooperative staff members were asked to provide lists of local cooperatives that they felt were typical of large, medium, and small locals in their trade areas. From these lists, nine local cooperative members of each regional were selected to be included in this study. While the regionals were allowed to provide their own criteria, classifications were based generally on total sales volume of farm supplies. In region B, this method resulted in a clear grouping of the locals. However, in region A, the average medium local was not much larger than the average small local. Thus meaningful comparisons could be made only between large locals and small groups.

Basic Information

The number of local cooperative members in each size category was about the same in the two regions. Large cooperatives averaged over 2,000 members, medium cooperatives about 1,000, and small cooperatives about 800 (table 1). Locals in region B tended to have larger boards, probably a reflection of having more branches that, in many cases, used to be autonomous cooperatives.

The average local in region B had about twice the number of branches as locals in region A in the same size category.

The number of employees varied directly with size. Locals in region B average more employees in all size categories, likely a reflection of having more branches and significant grain marketing programs. Supply sales per employee were about the same in both regions and in all size categories, averaging about \$220,000.

Sales

Local cooperatives in both federated systems and of all sizes experienced significant change in marketing and supply sales volume between 1981 and 1985 (table 2). Taken together, the locals experienced declines in dollar volumes in both supply sales and grain marketing. Total sales of 18 local cooperatives averaged \$15.6 million in 1985, down 5 percent from \$16.5 million in 1981. For all locals, supply sales were off 4 percent, and marketing sales fell 7 percent between 1981 and 1985. Locals in region A suffered large declines in grain marketing (down 27 percent), which led to a 10-percent decline in total sales. As a group, locals in region B nearly held their own in dollar terms, experiencing only modest declines. In both regions, wide variation among locals in sales volume changes is evident.

Use of dollar volumes masks, however, the true performance of the local cooperatives and implicitly of their regionals. Between 1981 and 1985, feed and food grain prices fell 13 and 20 percent, respectively. Of the major volume farm supplies, only chemicals experienced

price increases. Prices paid by farmers for feed, fertilizer, and fuels fell by 13, 6, and 6 percent, respectively. Thus, it appears that many of the locals may have achieved increases in physical volume handled for a number of supplies and farm products.

Large locals in region A showed a 44-percent decline in marketing sales, a 14-percent decline in supply sales, and an overall decline of 23 percent in total sales to 1985. Medium locals, down in marketing sales, were up 10 percent in supply sales for a 2-percent total gain. Small locals in region A were up 26 percent in supplies, 50 percent in marketings, and 26 percent in total sales.

Large locals in region B increased marketings by 12 percent, more than offsetting the 4-percent decline in supply sales. Both medium and small locals in region B experienced moderate declines in supply sales and large declines in grain marketings.

Locals of region B had advantages in grain marketing over large locals in region A, including (1) more clearly defined local trade areas, (2) better and larger grain handling facilities, (3) very limited intercooperative competition, and (4) strong grain marketing orientation.

Locals of region A were essentially farm supply cooperatives, with supply sales accounting for 75-80 percent of total sales. For most of these cooperatives, grain marketing was a sideline activity undertaken primarily as a service to members or in support of their feed operations. Generally they were not equipped with facilities or personnel to market grain effectively and to compete in marketing with other cooperatives, independent handlers, and grain companies.

Table 1—Size and structure of member locals, 1985

Item	Region A			Region B		
	Large	Medium	Small	Large	Medium	Small
<i>Average</i>						
Voting members	2,103	1,107	897	2,567	1,036	711
Board members	8	7	6	13	9	7
Number of branches	3	2	1	6	4	2
Number of employees	50	24	15	67	35	19
Supply sales (millions)	10.5	4.3	4.3	14.6	8.6	4.4
Marketing sales (millions)	2.8	1.5	0.6	29.7	8.1	4.3

Product Sales

Basic farm supplies sold to farmers by cooperatives are included in five groupings in table 3. Feed and fertilizer declined both in price and volume from 1981 to 1985, while chemical sales increased for locals in both regions. The leading product sold in both regions was petroleum, followed by fertilizer. In large locals, feed exceeded fertilizer sales (table 3).

Average product sales were down 2 percent in region A and 5 percent in region B from 1981 to 1985. However, grain marketing fell 31 percent in the lighter grain marketing areas of region A, while declining only 3 percent in the heavier grain marketing areas of region B. Total supply and marketing sales were down 10 percent in region A and down only 4 percent in region B from 1981 to 1985.

Financial Condition

Both total assets and total liabilities declined between 1981 and 1985 for the average local in regions A and B (table 4). Net worth of the average cooperative in region A increased by 13 percent and increased by 2 percent in region B. Net savings fell about 20 percent for locals in both regions. The fall in net savings was attributable to decreased patronage refunds from regional cooperatives. Operating margins at the local level held fairly steady. As a result, cash paid and equity revolved also fell considerably.

Smaller locals in both regions appeared to have fared better than larger local operations between 1981 to 1985 (table 5). Small cooperatives in both regions increased net savings, operating margins, net worth, and cash payments to farmers. Net worth was up for all local groups except

Table 2—Total cooperative sales of member locals, 1981 and 1985

Size and type	Region A			Region B		
	1981	1985	Change	1981	1985	Change
	--- Million ---		Percent	--- Million ---		Percent
Large:						
Supply	12.2	10.5	- 14	15.2	14.6	- 4
Marketing	4.9	2.8	- 43	26.5	29.7	+ 12
Total	17.1	13.3	- 22	41.7	44.3	+ 6
Medium:						
Supply	3.9	4.3	+ 10	9.1	8.6	- 5
Marketing	1.8	1.5	- 17	10.7	8.1	- 24
Total	5.7	5.8	+ 2	19.8	16.7	- 16
Small:						
Supply	3.4	4.3	+ 26	4.8	4.4	- 8
Marketing	0.4	0.6	+ 50	6.0	4.3	- 28
Total	3.8	4.9	+ 29	10.8	8.7	- 19
All cooperatives:						
Supply	6.5	6.4	- 2	9.7	9.2	- 5
Marketing	2.4	1.6	- 33	14.4	14.0	- 3
Total	8.9	8.0	- 10	24.1	23.2	- 4

midsize locals in region B. Operating margins increased for large locals in region A, midsize locals in region B, and small locals in both regions. Total assets were lower in 1985 for large locals in both regions, but liabilities were reduced, accounting for a slight increase in owners equity from 1981.

The financial showing of small locals may be attributed to increased sales volume in 1985 and lower operating costs. Midsize and large locals showed declining sales in supplies and grain, except for a slight increase in grain

marketed by large locals in region B. Reduced patronage refunds from regionals generally affect larger locals, which depend more on regional patronage to bolster net savings.

Facilities and Equipment

More branch locations and larger volumes of supplies handled and products marketed account for the increased numbers of facilities used to serve farmer members in region B. Generally, the number of facilities (table 6) and

Table 3—Average product sales for member locals, 1981 and 1985

Product	Region A			Region B		
	1981	1985	Change	1981	1985	Change
	--- Million ---		Percent	--- Million ---		Percent
Feed	1.29	1.12	- 13	1.20	1.07	- 11
Fertilizer	1.31	.99	- 24	2.93	2.80	- 4
Petroleum	2.32	2.60	+ 12	3.47	2.90	- 16
Chemicals	.47	.58	+ 23	1.10	1.46	+ 33
Supplies	1.09	1.07	- 2	1.03	.96	- 7
	6.48	6.36	- 2	9.73	9.19	- 5
Grain marketed	2.39	1.64	- 31	14.40	14.03	- 3
Total	8.87	8.00	- 9.8	24.13	23.22	- 3.8

Table 4—Financial condition of member locals, 1981 and 1985

Region	Region A			Region B		
	1981	1985	Change	1981	1985	Change
	--- Million ---		Percent	--- Million ---		Percent
Total assets	4,671	4,413	- 5.6	6,311	5,127	- 18.7
Total liabilities	1,976	1,349	- 31.7	3,060	1,804	- 41.1
Net worth	2,702	3,065	+ 13.4	3,251	3,323	+ 2.2
Operating margin	187	192	+ 2.7	97	92	- 5.1
Patronage from the regional	137	55	- 59.8	68	41	- 39.7
Net savings	324	247	- 23.8	165	133	- 19.4
Cash paid to members	69	42	- 39.1	28	7	- 75.0
Equity revolved	47	42	- 10.6	68	30	- 55.9

equipment (table 7) varied in proportion to size of locals in both regions.

Trade and Service Area

The size of a local's trade and service area depends on many factors, including products handled and marketed, cooperative and other competition, density and size of farms, and services provided for farmers by the local. Trade territories in region A were slightly larger than in region B for most product categories (table 8). In region B the larger locals tended to have larger trade territories, while in region A, size did not appear to be a factor in the extent of the trade territory.

Cooperative managers frequently strive to have their cooperatives grow by serving more farmers in extended trade areas or providing more services through the local. In region A, the high level of competition between cooperatives appeared to also motivate managers to extend their trade territories in an effort to capture volume adequate to ensure efficient use of their facilities.

Trade Area Competitors

Cooperatives in both regions experience similar levels of competition in terms of numbers of noncooperative competitors (table 9). In region A, locals encounter a considerably higher degree of competition from other

Table 5—Change in financial condition from 1981 to 1985 by size of local

Item	Region A			Region B		
	Large	Medium	Small	Large	Medium	Small
<i>Percent</i>						
Total assets	-15	+ 3	+ 28	-21	-18	- 12
Total liabilities	-39	-26	+ 10	-47	-35	- 28
Net worth	+ 6	+17	+ 37	+ 4	- 2	+ 1
Operating margins	+10	-29	+ 53	-67	+10	+ 73
Patronage from regional	-67	-68	- 17	-48	-27	- 79
Net savings	-23	-45	+ 23	-58	- 1	+583
Cash paid to members	-57	-35	+ 6	-67	-92	+150
Equity revolved	-35	+ 7	+227	-43	-79	+100

Table 6—Cooperative facilities by size of local, 1985

Facilities	Region A			Region B		
	Large	Medium	Small	Large	Medium	Small
<i>Number</i>						
Warehouses	18	13	4	23	10	10
Feed mills	9	3	1	12	5	4
Fertilizer plants	6	4	2	16	10	6
Petroleum depots	9	4	2	8	4	3
Petroleum stations	3	3	3	5	7	1
Supply stores	8	3	3	8	8	4
Total	53	30	15	72	44	28

Table 7—Cooperative equipment by region and size of local, 1985

Equipment	Region A			Region B		
	Large	Medium	Small	Large	Medium	Small
<i>Number</i>						
Tractors	7	0	0	4	1	0
Trailers	9	0	0	13	8	0
Spreaders	28	22	12	45	40	39
Sprayers	13	4	6	39	4	8
Applicators	37	20	24	60	32	39
Bulk trucks	29	17	15	65	31	19
Other trucks	66	34	10	84	40	21
Total	189	97	67	310	156	126

Table 8—Extent of trade area by size of local, 1985

Product	Region A			Region B		
	Large	Medium	Small	Large	Medium	Small
<i>Miles</i>						
Feed	18	15	20	12	12	11
Fertilizer	17	24	13	12	13	10
Petroleum	17	25	19	18	17	12
Chemicals	17	23	10	12	8	10
Supplies	18	25	10	12	8	9
Services	17	23	20	18	10	8
Average	17	21	15	14	12	10

Table 9—Cooperative and other local competition in trade area, 1985

Product	Region A						Region B					
	Large		Medium		Small		Large		Medium		Small	
	Coop	Other	Coop	Other	Coop	Other	Coop	Other	Coop	Other	Coop	Other
	Number											
Feed	2	7	2	3	2	4	0	4	0	7	1	7
Fertilizer	2	3	2	5	2	3	0	7	2	4	1	4
Petroleum	2	5	2	7	3	8	0	5	2	4	0	3
Chemicals	2	3	2	5	2	5	0	7	2	5	1	4
Supplies	2	9	2	7	2	7	0	6	1	8	1	7
Services	2	10	2	7	2	7	0	6	1	7	1	3
Average	2	6	2	6	2	6	0	6	1	6	1	5

cooperatives in all supply groups. Locals in region A have at least two competing cooperatives, and to many managers these represent the focus of their competitive effort. In region B, much of the competition between cooperatives is limited to fringe areas of a cooperative's territory.

Competition among suppliers of farm products helps to keep prices in line and services responsive to the needs of farmers. However, when the competitors in a trade area are cooperatives, they duplicate services, increasing operating costs at their members' expense. In both regions, it appears clear that a healthy competitive environment would remain even if competition between cooperatives were eliminated.

Each local cooperative in region A was in competition with two other locals and six independent competitors. In addition, several regional cooperatives were competing for the retail business of locals, duplicating services and costs which increased costs to farmers. In some situations, only the strong loyalty of farmer members to their cooperative and support services provided by the regional enabled locals to overcome the costs associated with intercooperative competition and stay in business.

Shares of the Market

Local managers were asked to estimate the share of the market held by their cooperative in their primary trade areas for each major supply group. Averages of these estimates are reported in table 10. Among all supply categories the 18 locals involved in the study had an average 32 percent of the share of the farm supply market within their trade territory.

On an average, the larger locals were able to obtain larger shares of the various supply markets than smaller locals. This performance was consistent among the four bulk supply categories: feed, fertilizer, petroleum, and chemicals. In general supplies and services, the comparative advantage of the larger locals in obtaining market share appears to be diminished.

Taken as a group, locals in both regions achieved about the same level of market penetration. There were some minor differences between the two regions in some products. Locals in region B had larger shares of the petroleum market, while locals in region A appeared to do better in chemicals and services. From this it may be inferred that the heavier cooperative competition in region A did not affect the ability of individual cooperatives to gain market share relative to the lighter cooperative competition in region B. What cannot be inferred is whether the heavy intercooperative competition was a limiting factor on the ability of locals in region A to obtain an even larger share of the supply market.

In assessing what is needed to improve their competitive position, local managers pointed to the need for a careful reading of farmer needs and community services to examine possible realignments of products and service offerings. Local managers believe that in order to improve operations, sales, and services and, hence, market share and profitability, they must put an end to the philosophy of providing for the needs of the few at the expense of the many. They believe that cooperative members must begin to pay for the services they receive but be able to pick those that they need.

Table 10—Cooperative share of market for large, medium and small locals, 1985

Product	Region A			Region B		
	Large	Medium	Small	Large	Medium	Small
<i>Percent</i>						
Feed	47	33	15	33	27	28
Fertilizer	50	38	29	45	40	40
Petroleum	42	33	27	50	37	42
Chemicals	45	33	32	33	30	26
Supplies	17	25	18	27	22	19
Services	34	38	25	30	25	21
Average	39	33	24	36	32	29

Managers felt that the major weaknesses in their organizations were internal management practices, communications, and decisionmaking practices. Improvement in these areas could greatly enhance the ability of locals to take on their competition, improve cost performance, and gain market share.

Meeting and surpassing the competition was the theme running throughout manager discussions on how to gain market share. Managers of larger locals listed services first and suggested offering a financial service package to large customers as the way to gain more sales. Managers of midsize locals noted credit policies, services, and salesmanship as the way to gain sales. Managers of smaller locals felt they must improve facilities, price right, select the right people, and present a favorable image of service to the farmer and the public at all times.

USE OF REGIONALS BY LOCAL COOPERATIVES

Local cooperatives established regional cooperatives to purchase supplies in volume at lower prices, provide market outlets, and undertake various manufacturing and distribution functions. Member locals were committed philosophically to purchase nearly all of their products and services from the regional. For many years the system worked well. Beginning in the 1970's, this commitment waned on the part of some locals due to a number of factors. The growth of regionals in terms of territory and complexity eroded local cooperatives' identification with their regional. Financial stress and increased competition for lucrative accounts caused many locals to place higher priority on local savings than on regional loyalty and to opt for alternative sources of supplies.

Lower use of regionals by member locals affected operating efficiency at the regional at the time farmers were already cutting production levels. Declining inflation and lower prices adversely affected cash flow needed to cover some earlier questionable investment decisions by regionals. The image of regionals was damaged in the eyes of many locals and farmers who questioned their continued ability to effectively serve member locals.

This study indicates a major refocusing by regionals on how to better align their organizations and the cooperative system as a whole to strengthen local cooperatives and their ability to serve the farmer. The willingness to explore and adopt new structures and changed relationships between the locals and their regionals is very much in evidence.

Function and Services of Regional Cooperatives

Both regionals in the study have been involved in providing supplies and services for local cooperatives and farmers for over 50 years. Regional A has provided quality supplies and services to more than 1,000 member locals in the multistate trade area. Regional B focuses its operations in a single State serving a smaller number yet larger volume group of member locals. It has extensive involvement both in the provision of farm supplies and in grain marketing.

Through a combination of ownership in affiliated interregionals and subsidiaries and investment in their own manufacturing facilities, the two regionals have increased the buying power of farmers. Joint ownership with other regionals of research and manufacturing facilities in plant foods, chemicals, seed, and feed enables the regional to supply top quality products at competitive prices to member locals and farmers. Through their regionals, farmers own oil refineries, export elevators, feed mills, pipelines, extensive warehouse and transportation systems, and sophisticated agronomic advisory services. Farmers' investment in the cooperative system provides access by truck, rail, barge, and vessel to domestic and world grain markets. Product brand names have been adopted to improve cooperative image, recognition, promotion, and sales.

Federated regionals have always been more than just providers of products and services for local cooperatives. From the beginning, they established education and training programs for local as well as regional board members, managers, and staff employees. They provided health insurance, retirement programs, and property insurance programs for member locals. From recordkeeping to financial analysis of local operations, regionals offered capabilities and management services to interested locals.

Today federated regionals are involved with locals and farmers providing a vast array of expert and technical assistance in nearly all aspects of farming and local cooperative operations. The regionals maintain professional staffs of knowledgeable and experienced people to work directly with locals in providing management consulting services. Computerized analyses of local operations enable staff to communicate information to assist local managers in their operations.

Regional field staffs visit and consult with locals and farmers on crop and plant food technology while working

to increase the sales potential of store merchandising. Commodity and field representatives serve member locals in technical training, sales, and services, and encourage system changes to meet the changing needs of farmers, improve operations, and enhance the image of the local cooperative. Regional assistance may be requested by member locals in their search for experienced managers and employee replacements.

Source of Regional Supplies

The two regionals, like other federated regionals, manufacture some products, purchase available products from interregional cooperatives, and purchase supplies from outside the cooperative system. As regional cooperatives and cooperative systems in the Nation have grown and extended vertically, the ability of cooperatives as a group to provide for their own needs has increased. Today, fewer products are purchased outside the system. Regionals are manufacturing more of the main products needed by locals to serve farmers.

Together, the two regionals manufactured 45 percent of the supplies they distributed to locals. An additional 23 percent was purchased through interregional cooperatives. The remaining 32 percent came from noncooperative sources.

The vast majority of feed, petroleum, fertilizer, and seed acquired by the two regionals was manufactured by the regionals themselves or came from interregional cooperatives. Of these products, only fertilizer and seed were partially purchased from noncooperative sources. Noncooperative firms were the primary suppliers of farm

chemicals, hardware, and store supplies. However, a significant share of store supplies did come through interregionals.

Source of Local Supplies

Purchasing supplies from regionals by member locals depends upon several factors: (1) buying power of the local, (2) prices from alternative sources relative to regional price, (3) delivery costs, (4) local use of regional services, and (5) regional involvement in local operations. In making their purchasing decisions, local managers must consider these factors in light of their responsibility to act in the interests of their members and to ensure the financial viability of their organizations.

Locals in both regions have quite similar purchasing patterns (table 11). Locals in regions A and B purchased 80 and 83 percent, respectively, of their total supplies from their regional cooperatives. Noncooperative suppliers accounted for 14 and 15 percent of total supplies purchased.

The size of the local had no clear effect on their decisions as to source of supplies. If anything, data from the two regions suggest opposite interpretations. Large locals in region A purchased 68 percent of their products from regionals, 58 percent from their main regional and 10 percent from other regionals. In contrast, large locals in region B purchased 87 percent of their products from their main regional and only 1 percent from other regionals. This provides evidence of the nature of competition between regional cooperatives in region A.

Table 11—Source of supplies by size of local, 1985

Size of local	Region A			Region B		
	Purchased from			Purchased from		
	Manuf. by local	Regional	Noncoop	Manuf. by local	Regional	Noncoop
<i>Percent</i>						
Large	14	68	18	3	88	9
Medium	1	88	11	2	84	14
Small	4	83	3	1	79	20
Average	6	80	14	2	83	15

Large locals in region A were the only group purchasing an appreciably lower proportion of their needs from the regional cooperative. This difference is due primarily to their own manufacturing activities rather than a leakage from the cooperative system. Large locals in region A also purchased more from outside the cooperative system than other locals in the region. A possible reason could be that these locals, having learned to seek offers from several regional cooperatives, extend their philosophy of searching for alternative suppliers to noncooperatives as well. Data may also suggest that the business of the larger locals in region A may be more heavily sought by both cooperative and noncooperative suppliers.

Moving Supplies to Locals

Providing and delivering products and services to locals and farmers has traditionally been a major strength of the cooperative system. At one time, delivery of products by the regional was considered a service to locals and was provided for most products. As costs of warehousing and delivery increased for the regional, alternative transportation methods were sought. Locals increasingly began to pick up supplies from distribution centers using their own vehicles. This became increasingly justified on the basis of cost as the volume purchased by locals grew. Cooperatives also turned increasingly to contract haulers.

About 41 percent of products purchased by locals in region A were delivered by the regional, 27 percent were picked up by locals, and another 27 percent were transported by contract haulers. Small and medium locals in region A were far more dependent on their regional for delivery of their products (57 and 44 percent) than were

large locals (23 percent). Large locals in region A picked up 45 percent of their supplies using their own vehicles.

Locals in region B were far less dependent on their regional for delivering supplies, receiving an average 12 percent through regional deliveries. They picked up more on their own (40 percent) and contracted more (45 percent) than locals in region A. Thus, in this smaller geographic area and in light of a greater number of branches or receiving points, locals in region B have assumed far greater responsibility for directing the flow of products coming into their facilities.

Delivery of Services to Farmers

Farmers look to local and regional cooperatives to provide a range of services. For many services, locals and regionals share responsibility for providing and delivering these services to farmers. Recent trends toward increased emphasis on cost recovery and alignment of charges to the direct users of services have caused many cooperatives to separate the cost of services from basic product prices. Charges for many of these services were formerly included in product prices.

Local managers were asked to indicate whether the local, regional, or both took responsibility for providing a range of functions and services and how the costs of providing those services were covered. The functions and services included the following:

1. Feed manufacturing
2. Feed delivery
3. Selling of fertilizer elements

Table 12—Transportation of products to locals by size, 1985

Size of local	Region A				Region B			
	Picked up by local	Delivered by			Picked up by local	Delivered by		
		Regional	Other Coop	Contract		Regional	Other Coop	Contract
Percent								
Large	45	23	8	24	43	7	1	49
Medium	13	44	7	36	63	20	0	17
Small	22	57	1	20	13	10	7	70
Average	27	41	5	27	40	12	3	45

4. Fertilizer blending
5. Fertilizer application
6. Bulk fuel depot
7. Bulk fuel delivery
8. Retail fuel pump outlet
9. Chemical application
10. Agronomic testing
11. Auto and tires, batteries and accessories
12. General farm supplies
13. Farm management consulting
14. Other services

The division of responsibility between the locals and regionals for providing these functions and services were essentially the same for the two regions. In both, the regional provided about 22 percent of the services (table 13). Services such as farm management analysis, seed and soil testing, and chemical and pesticide recommendations were generally provided by the regional.

Locals in region A included service costs in price in 67 percent of services and added extra charges for 33 percent of services. Locals in region B included cost in price in 57 percent of services and added extra charges for 43 percent of services provided farmers. The greater degree of intercooperative competition in region A may have the effect of slowing actions to establish separate charges for services. Differences in the service charge practices between locals of various sizes do not provide clear meaning or interpretation.

INVOLVEMENT OF REGIONAL COOPERATIVES IN LOCAL OPERATIONS

Federated regional cooperatives formed by local cooperatives to serve member locals generally provided the services needed without little direct authority or control over locals. The system promoted farmer control and allowed local boards and managers to determine operating policies to serve local farm needs. For a long time, cooperatives followed a theme of service to all—often at the expense of operating efficiency. Recent changes sweeping agriculture, in farming and agribusiness, have demanded maximum operating efficiency of the whole cooperatives' system. Regionals have accepted the challenge and are taking a leadership role in promoting involvement in local operations as a step in developing an effective system for delivery of products and services to farmers.

Local managers of large, medium, and small cooperatives were nearly unanimous in saying that farmers were better served if regionals were more involved in local operations. They expressed strong confidence in the ability of their regional to serve member locals. Managers were divided as to whether they felt involvement by the regional in local operations should be properly initiated by the local or regional. However, they believed, by a 2-to-1 margin, that the regional was more likely to initiate involvement in local operations.

By a 2-to-1 margin, local managers thought regionals should get more involved in local management, while the

Table 13—Cooperative system services provided by size of local, 1985

Size of local	Region A				Region B			
	Service provided		Inc. in price	Extra charge	Service provided		Inc. in price	Extra charge
	Local	Regional			Local	Regional		
Percent								
Large	79	21	57	43	82	18	64	36
Medium	83	17	58	42	75	25	58	42
Small	73	27	82	18	75	25	50	50
Average	78	22	67	33	77	23	57	43

minority thought the level of involvement should stay about the same. Selection of local cooperative managers was a specific area that managers indicated the need for greater regional involvement. Many suggested that regionals recommend candidates for managers to local boards of directors. Several said that the regional should direct the hiring of a local manager, and more than half indicated that the regional should influence the decision of selecting a manager. Most, however, wanted the local board to make the final decision.

The majority of member locals believed that they should be affiliated with and purchase most of their products from one regional, even though they might, from time to time, purchase from another regional or noncooperative supplier. Demonstration of loyalty to one regional should inspire regional loyalty in return and promote better service and efficiency in the long run. While some local managers felt that competition between regionals helped keep prices in line, most said that the costs of maintaining duplicated services outweighed any possible competitive benefits.

Level and Nature of Involvement

Regional involvement in member local operations reflects the working relationships established between the regional and each member local. It represents communication and exchange of information within a productive environment growing between regional staff and local management. Contributions to the success of the cooperative system are made by the local and regional organizations who recognize the value of communication and a close working relationship. When member locals make their needs known, the staff of the regional can respond with information, advice, and recommendations. As involvement develops, the two levels of operations become a coordinated working system to serve farmers.

Local managers were asked to estimate the level of regional involvement in ten areas of local operations or activities. The level of regional involvement was rated by local managers using a 0-to-4 scale with a rating of 4 meaning "highly involved" and a rating of 0 meaning "not at all involved." Average ratings given by managers in the three size categories are given in table 14.

Ratings by local managers indicated the highest level of regional involvement in local operations was in the areas of product sales, personnel training, and product information. The lowest level of regional involvement was

in the areas of credit policy, personnel selection, and operating efficiency. Although larger locals indicated a slightly lower level of involvement by regionals, ratings of involvement in the various areas of operations were quite consistent among all cooperatives in the study. These ratings closely follow involvement findings in the local-regional relationships.¹

The assessment by regional cooperative managers of their cooperatives' involvement in local cooperative operations was generally consistent with local manager ratings. Regional managers indicated several factors or conditions which lead to increased involvement by their regional. These include small size, poor financial condition, weak managers, and a weak local board of directors. They indicated that their regionals do not increase their level of involvement in local operations when the local's problem relates to inadequate facilities or physical plant. They also indicated a strong aversion to increasing involvement when a high level of independence and autonomy is clearly preferred by a particular local.

Regional involvement has increased in the past 5 years, according to regional managers. They expect this trend to continue. Increased communication capabilities, leadership expertise, and regional development of programs to support local operations are reasons for regionals to be more involved in local management. On the other side, the operating problems of many locals, from lower volume to higher costs and inefficiency, signal the need for more help from the regional in today's changing agricultural economy.

Regional Personnel Involved

Regional personnel have always been involved, one way or the other, in member local operations. In past years, financial problems of the local were frequently the only impetus for regional involvement in local cooperative operations. Changing economic pressures have forced a trend away from complete independence and autonomy of local and regional management functions to a shared system to gain efficiency and compete in the market place. In practice, this sharing of responsibility involves the working relationship between specific individuals from the regional and the appropriate local personnel.

¹Local-Regional Cooperative Relationships in the Midsouth, ACS Research Report Number 59, 1987, Lloyd C. Biser and John R. Dunn.

Local managers were asked to rate the level of involvement by various regional cooperative staff members in their operations. As before, a 0-to-4 scale was used with a rating of 4 meaning "highly involved" and a rating of 0 meaning "not at all involved." Average ratings for a variety of regional job classifications are given in table 15.

Local managers indicated the highest level of involvement was in training specialists, field personnel, and

information specialists. This is consistent with the type of operations or functions in which the greatest level of regional involvement was seen. The lowest level of involvement was with regional board members, telecommunications specialists, and division heads. Given the increasingly technical requirements of communications and the increased computer linkages between regionals and locals, the involvement of regional telecommunications and computer specialists can be expected to increase.

Table 14—Local managers estimate level of regional involvement in each of 10 activities by size of local

Cooperative Activities	Size of member local			All locals
	Large	Medium	Small	
	<i>Average rating¹</i>			
Product purchase	2.3	2.5	1.5	2.1
Product service	2.0	2.5	1.5	2.0
Product sales	2.2	3.0	2.2	2.4
Product information	3.0	3.5	3.2	3.2
Advertising	1.8	2.7	2.0	2.2
Financial policy	2.0	2.2	2.8	2.3
Personnel selection	1.3	1.8	1.7	1.6
Credit policy	1.2	1.7	1.5	1.4
Operating efficiency	1.8	2.0	1.7	1.8
Personnel training	2.5	3.3	3.0	2.9
Average: All activities	2.0	2.5	2.1	2.2

¹Rated on a 0-4 scale where 4 means very influential and 0 means not at all influential.

Table 15—Local managers estimate involvement of regional personnel

Regional personnel	Size of member local			All locals
	Large	Medium	Small	
	<i>Average rating¹</i>			
Regional board	0.0	0.8	0.5	0.4
Regional manager	1.0	2.3	1.7	1.7
Division heads	0.8	2.2	2.8	1.9
Field personnel	2.0	2.7	2.7	2.5
Product specialists	2.2	2.5	2.3	2.3
Training specialists	2.5	2.8	2.5	2.6
Information specialists	2.5	2.8	2.2	2.5
Management specialists	2.7	2.2	1.8	2.2
Telecomm specialists	1.3	1.8	1.2	1.4
Other specialists	1.0	1.5	2.0	1.5
All regional personnel	1.6	2.2	1.9	1.9

¹Rated on a 0-4 scale where 4 means very influential and 0 means not at all influential.

Ratings by locals in the three size groups were fairly consistent for most regional job classifications. Larger locals indicated a relatively lower level of involvement by regional field personnel, likely a result of locals having a greater level of product expertise represented on their own staffs. On the other hand, the greater complexity of managing larger local cooperatives has led, apparently, to a relatively higher level of involvement by regional management specialists in large local operations.

RESTRUCTURING COOPERATIVES

Farmers long believed that farmer cooperatives, owned and controlled by farmers, could offset industrial and political power in the marketplace and assure a fair return. Cooperatives proved their worth by providing many of the products and services needed and used by farmers. Cooperatives grew and expanded services, gaining market share in a growing domestic and world market.

In the 1970's, farmers and cooperatives tooled up to feed the world and compete in a world agricultural market. However, rapid adoption of modern agricultural methods helped many nations gain self-sufficiency and become, in some cases, net exporters of farm products. Inconsistent farm policies, grain embargoes, and trade barriers helped reduce and close world market opportunities. Investments by cooperatives based on export-driven markets turned sour.

The net effect has been the maturation of the U.S. grain market and associated markets for farm supply. Growth could no longer be counted on as the remedy for operating efficiency, excess capacity, or suboptimal performance. Farmers and their cooperatives were required to regroup and restructure operations to successfully compete in a more demanding marketplace. The two federated systems responded to this challenge to more effectively serve member locals and farmers.

Interregional Joint Venture - Regional A

In an effort to respond to the problems of overinvestment and duplication of effort at the regional and local levels, regional A entered into a joint venture with a competing regional cooperative system. Impetus for the precedent-setting agreement came from farmers, ranchers, local directors, and managers who urged their regional organizations to explore more effective ways to serve farmers. Member locals told their regionals that responding to the changing farm economy would require a

willingness to work together, a willingness to change, and a long-term commitment to cooperation.

Under the agreement, each regional was assigned responsibility for a major supply line in which they had a relative advantage. One took over full responsibility for feed operations throughout the joint trade territory while the other took full responsibility for petroleum and fuel marketing and distribution. Agronomy operations, including fertilizers and farm chemicals, were assigned to a new entity created by the agreement. The new entity will act as an agent for the two regionals. Each regional will be charged for purchases and expenses and be credited with sales on a 50-50 basis. All properties needed for the operation of the joint venture will be transferred to it at book value.

By increasing the scale of operations in these major supply groups, operating efficiency will be improved and administrative costs greatly decreased. In addition, regional competition will be limited and duplication of services eliminated in many areas. Thus, by a single agreement, a major step toward improvement of the overall cooperative system and elimination of destructive intercooperative competition was taken.

Membership Agreement and Service Program - Regional B

To promote closer working relationships with all member locals and improve the system's operational efficiency, regional B's board recently adopted a new membership agreement and service program with member locals. In substance, the regional confirms a commitment to make every effort to supply the products and services and to gain markets for local cooperatives. It agrees to be competitive with major suppliers in pricing and service, in cash grain bids and marketings, and in charges for services provided for locals. With member commitment, it agrees to help make operations more efficient and competitive in the marketplace.

Each local member of the association, upon signing the agreement, agrees to make every effort, when economically feasible, to maximize its purchases of products and services and to use marketing facilities of the association. Each member agrees to abide by the rules, regulations, and directives of the association. Each member also agrees to pay for services and merchandise furnished on terms established by the association and to employ its manager from candidates approved by the association.

The regional seeks and plans to get more involved in operations of member locals. Plain and simple, the purpose is to improve operations at committed locals, to upgrade facilities and to provide every resource needed to make member locals more competitive. This two-way commitment asks locals to work more closely with the regional in an effort to be more competitive as individual units and to strengthen their cooperative system as a whole.

Summary: Local-Regional Strategies for Change

The federated regionals in the study moved in different directions to adjust to changing conditions. In both cases, actions were taken in direct response to what was perceived to be the greatest competitive weakness of the individual federated systems. Regional A, being in an area of considerable duplication of cooperative facilities, undertook actions to rationalize cooperative assets through joint efforts with other cooperatives.

In regional B, competitive problems were diagnosed as arising from an inadequate level of coordination between the local and regional levels. The response in this case was adoption of a more strict membership agreement and services program designed to increase the flow of goods and services remaining within the cooperative system. The intended result was a more efficiently utilized and, therefore, more competitive regional-local system.

Managers of member locals believe their cooperatives got to their present position by providing the products and services needed by farmers at the best terms possible. They expect to continue to serve farmers with a strategy that mirrors the needs of the successful farmer, both large and small, whose bottom line is operating efficiency. Locals need a responsive regional to effectively serve their needs in pursuing this end.

In many federated systems, a close working relationship between the regional and local has provided a coordinated operational system for fulfilling needs of the farmers. They have been successful because management of the regionals is committed to serving member locals in ways that only farmers benefit. The emphasis on local achievement, encouraged through heavy regional involvement, seems to be a key to successful system operations.

Commitment to change by all levels of federated cooperative systems, including locals, regionals, and interregionals, is needed. The types of needed change will

take many forms, including improvement in system controls, elimination of unnecessary physical and financial levels or steps in the system, and increased facility utilization through elimination of duplication. The need to evaluate, plan, and restructure for change is ongoing, and will continue for the simple reason that efficient operating systems are demanded.

Cooperative strategy to meet this challenge will stress that investments, affiliations, research and development, operations, and services be directed to improving the farmer's standard of living. From the beginning, farmers working together formed cooperatives to achieve their economic goals. While much has changed, this basic objective is no different today.

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Agricultural Cooperative Service**

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Agricultural Cooperative Service (ACS) provides research, management, and educational assistance to cooperatives to strengthen the economic position of farmers and other rural residents. It works directly with cooperative leaders and Federal and State agencies to improve organization, leadership, and operation of cooperatives and to give guidance to further development.

The agency (1) helps farmers and other rural residents develop cooperatives to obtain supplies and services at lower cost and to get better prices for products they sell; (2) advises rural residents on developing existing resources through cooperative action to enhance rural living; (3) helps cooperatives improve services and operating efficiency; (4) informs members, directors, employees, and the public on how cooperatives work and benefit their members and their communities; and (5) encourages international cooperative programs.

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