NCR-194 Committee Meeting

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The Decision to Merge: A Case of U.S. Dairy Cooperatives

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Presentation Objectives

- Review Case of Dairy Cooperative Merger
- Present Methods for Analyzing Pre and Post Merger Financial Performance
- Propose a Set of Financial Ratios to Measure Impact of Merger
- Generate Discussion

JUSTIFICATION for STUDY

- Increasing Number of Mergers, Especially Dairy
- Larger Scale and Scope
- Having Greater Impact on Members
- Limited Attention Given to Case Studies of Dairy Mergers
- Need for Methodology to Evaluate Post Merger Performance

Objectives of Study

- Identify Motivation for Merger
- Review Criteria That Decision Makers Use to Evaluate Merger Option
- Identify Unique Barriers to Merger and How They Were Overcome
- Explore Approaches to Measuring Impact of Merger

Methods

- Developed Case Study Framework
- Designed Questionnaire for Structured Interview
- Interviewed Manager and Board Chairmen Involved in Merger Decision

Methods (cont'd)

- Reviewed Annual Reports and Financial Statements for Pre-merger and Post merger Periods

- Developed Set of Financial Ratios to Measure Performance Before and After Merger

DAIRY COOPERATIVE GROWTH DILEMMA

- Limited Strategies vs. Other Types of Dairy Firms
- Geography, Products, Processing, Gov. Affairs, Access to Capital, Size and Scope & Acquisition Potential
- (see Table 1.)

COOPERATIVES IN THE STUDY

- Eastern Milk Producers Cooperative
- Milk Marketing Inc. (before merger)
- Milk Marketing Inc (after the merger)

Cooperative Location & Membership

Member Areas	Number of Members
Eastern Milk Prod.	**3,200**
Headquartered in Syracuse, NY	
Members: PA, NY, VT, MD, DE, MA	
Milk Marketing Inc.:	**5,700**
Headquartered in Strongsville, OH	
Members: OH, IN, PA, KY, MD, MI NY, WV	

1995 Data

Cooperative Volume

Total Operating Revenue:

Eastern M.P.	$248,891,000
MMI	$323,464,000

Volume of Member Milk:

Eastern M.P	1.78 billion lbs.
MMI	3.82 billion lbs.

WHY MERGE?

- Changing Industry Structure
- Limited Growth Potential
- Increase Value-Added Activity
- Limited Equity and Access to Capital
- Becoming Global Market
- Spread Costs Over Larger Volume

BARRIERS TO MERGING

- Leaders Not Open to Considering Merger
- Loss of Identity and Control
- Unwilling to Take Risk Associated with Merger
- Directors Unwilling to Face Elimination of Their Board Seats
- Rotating Board Leadership Due to Term Limits

Financial Performance Areas

- Profitability
- Debt Capacity
- Return on Equity
- Cutting Expenses

Financial Ratios Pre and Post Merger

Ratio	Eastern	MMI pre	MMI post
Gross Margin	4.0%	6.2%	5.0%
Net Margin	.01%	.8%	.96%
Debt. Ratio	.67	.56	.66
Debt to Equity	.46	.09	.29
Return on Equity	.2%	7.0%	12.2%
Equity Redemption	11 yrs.	9 yrs.	7 yrs.
Expenses/cwt.	.55	.40	.36

POST MERGER PERFORMANCE

- Gross Margins Improved
- Net Margins Improved
- Significant Improvement in Return on Equity
- Reduced Estimated Time for Equity Revolvement
- Reduced Admin. Expenses/cwt.

LIMITATIONS TO CASE STUDIES AND RATIO ANALYSIS

- Case Represents Only 2 Cooperatives
- Cannot Make Statistically Valid Inferences
- Financial Statement Analysis Has Limited Value When Trying to Make Comparisons Across Firms or Industries
- Alternative Accounting Methods Can Make Comparisons Problematic
- However, Merger Application Valid

CONCLUSIONS

- There Are A limited Set of Strategic Options for Dairy Cooperative Growth
- Financial Statement and Ratio Analysis Can Measure Selected Performance Areas
- In the Case of Eastern M.P. & MMI:
  - Financial Performance Improved as Measured by Selected Ratios

SUMMARY

- Increased Incidence of Mergers Among Dairy Cooperatives
- Study Attempts to Improve Understanding of Need and Rationale to Merge
- Propose An Method to Measure Impact of Mergers
- Case Study Approach and Financial Ratio May Prove to Be Useful Analytical Tool
- Further Research on Impact at Member Level

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