



Evaluation of Cooperative Mergers: A Strategic and Financial Analysis Case Study

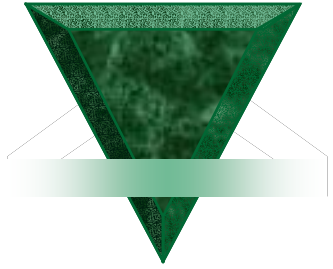
Dr. Joan Fulton

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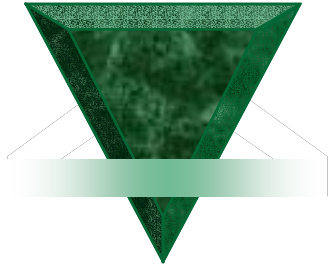
Challenges for Cooperatives

- ✔ As agriculture continues to industrialize, local cooperatives are being squeezed from two directions.
 - ✔ National and regional level cooperatives are pushing for efficiency.
 - ✔ Member patrons get larger, and can buy directly from the manufacturer



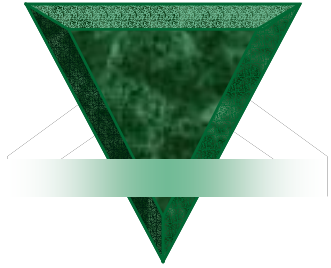
Challenges

- ✓ In some cases, a local cooperative has a choice of merger partners where
 - the management and directors must evaluate their different strengths and weaknesses.

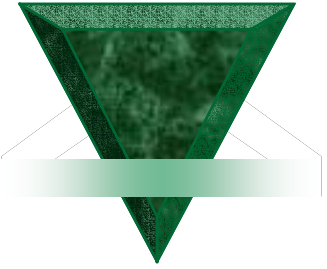


Research Project

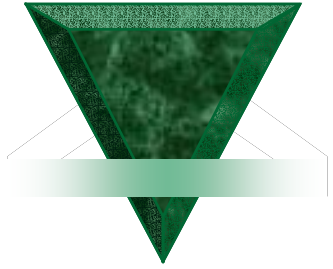
- As a result, a joint research project was developed between Colorado State University and Purdue University.
- We evaluated mergers/acquisitions and joint ventures/strategic alliances among local cooperatives.



- In-person interviews were conducted with the manager of locally owned farm supply/grain marketing cooperatives in Indiana and Colorado (35 in each state) in spring of 2000.

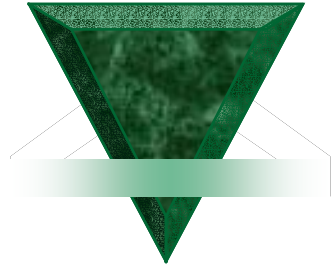


- ✓ Extensive information was obtained concerning
 - the driving forces behind the business reorganizations
 - the importance of various factors contributing to the success of the business reorganizations
 - the cooperative's financial position
 - the financial analysis that the cooperative used when evaluating business reorganizations.

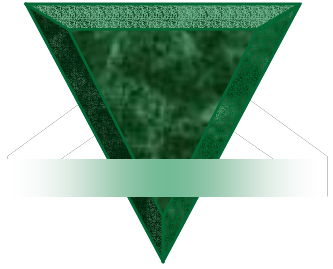


The Case Study

- ✔ Using this information, we developed a two part case study using
 - A hypothetical cooperative, Alton Valley
- ✔ This case is designed to be used in either the undergraduate classroom or in extension programming with cooperative managers and directors.

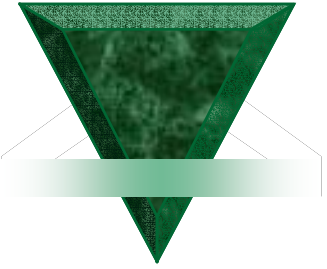


- ✔ Part I focuses on how to use financial analysis in business reorganization decisions.
- ✔ Part II focuses on how to analyze alternative business reorganization possibilities from a strategic management perspective.
- ✔ The two parts of the case are written in such a way that they can be used individually or together.



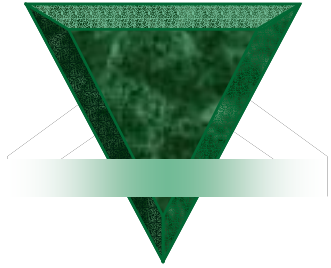
Background

- ✔ Alton Valley is a strong cooperative
 - Limited market territory
- ✔ Two merger possibilities; both with strong presence in the area:
 - Sedgewick Farmers Cooperative
 - NorthStar Ag.



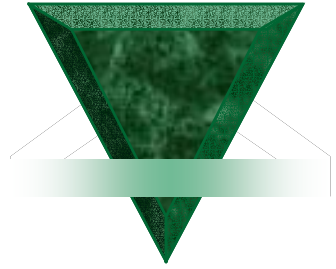
▼ Alton Valley:

- Loyal customer base
 - Especially with agronomy division
- Energy division growth
 - Urban development
- Grain business
 - Loss of crop acreage/fewer bushels of grain in elevators



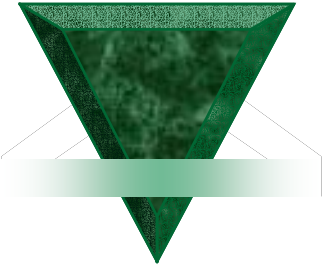
– Nontraditional lines of business

- Pet food
- Horse feed
- Lawn/garden business
- Bird feed
- Considering a C-store



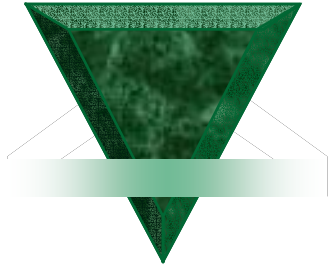
✓ NorthStar Ag.

- Large
- Strong agronomy and energy divisions
- Big player in regional grain trade
- Brings business diversity
- Heavy debt



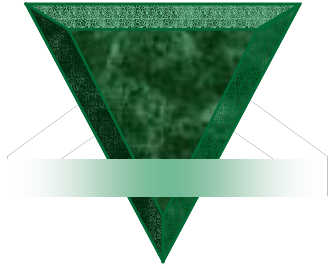
✔ Sedgewick Farmers Cooperative

- Large
- Agronomy division is the core business
- Grain division has rail facilities
- Feed division is virtually nonexistent
- Energy division very strong
- Focus on price over service
- Financially strong



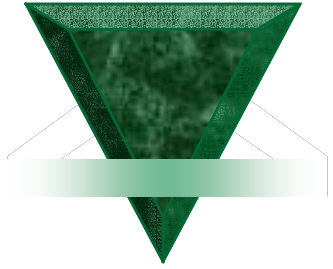
Structure and Format

- ✔ Students must ultimately decide which (if either) of the two potential cooperatives to partner with.
- ✔ An important feature of this case:
 - the decision is not clear-cut because both merger possibilities have strong and weak points.



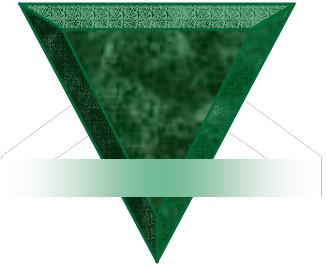
Part I: Financial Analysis

- ✔ This case is well suited for students who have had a basic class in agricultural finance.
- ✔ Could also be used as part of an agricultural business or cooperatives class
 - with the instructor providing background in basic ratio analysis.
 - This case could be used for a one-week section of a cooperatives class.
- ✔ Used for a day- long cooperative director-training program

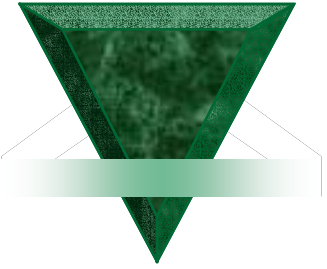


Financial Analysis

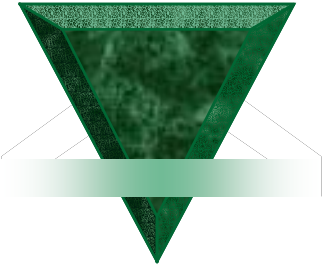
- ✓ Why Apply Financial Analysis
 - Set goals
 - Collect financial and economic information
 - Prepare financial statements
 - Measure financial performance



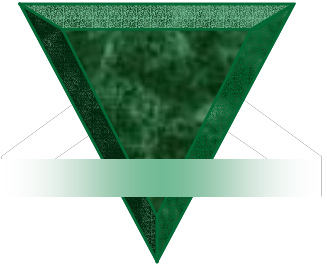
- ✓ Criteria for Measuring Financial Performance
 - Liquidity
 - Solvency or Debt
 - Profitability
 - Management Efficiency
 - Trends and Cross-Sectional Analysis



- ✔ Consider the profitability ratios for Northstar Ag. and Sedgewick Farmers Cooperatives.
 - Identify the strengths and weaknesses of these two cooperatives from a profitability perspective.
- ✔ Consider the management ratios for Northstar Ag. and Sedgewick Farmers Cooperatives.
 - Identify the strengths and weaknesses of these two cooperatives from a management perspective.



- ✔ Consider the liquidity ratios for Northstar Ag. and Sedgewick Farmers Cooperatives.
 - Identify the strengths and weaknesses of these two cooperatives from a liquidity perspective.
- ✔ Consider the debt ratios of Northstar Ag. and Sedgewick Farmers Cooperatives.
 - Identify the strengths and weaknesses of these two cooperatives from a debt perspective.

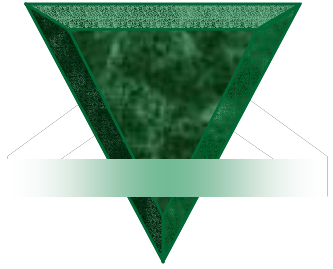


- ✓ Next compare all of these ratios with those of Alton Valley and discuss strengths and weaknesses.
 - What is the decision of the group?
 - Which is the merger partner, if any?



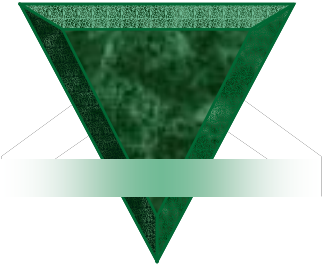
Ratio Table

	Northstar	Sedgewick	Alton Valley
Net Profit Margin	0.60%	1.54%	1.70%
Return on Assets	3.56%	5.34%	5.10%
Return on Equity	9.00%	9.00%	9.27%
Days Sales Outstanding	6.30	14.47	12.00
Fixed Asset Ratio	10.24	5.77	5.26
Total Asset Turnover	5.96	3.47	3.00
Current Ratio	0.90	1.50	1.37
Quick Ratio	0.25	0.57	0.98
Debt/Assets	60.44%	40.68%	45.00%
Equity Multiplier*	2.53	1.69	1.82

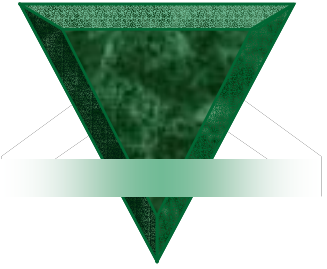


Part II: Strategic Analysis

- ✔ This case is well suited for students who have had a basic class in ag strategic management or a general business management class.
- ✔ Could also be used as part of an agricultural business or cooperatives class
 - with the instructor providing background in basic strategic management analysis.
- ✔ Used for a day- long cooperative director-training program

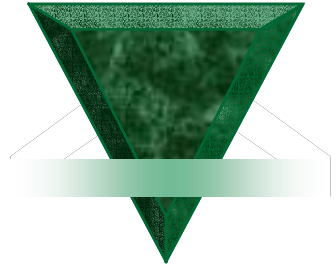


- ✓ The second case requires that the participants have an understanding of basic strategic management issues.
 - Perform a SWOT analysis for each of the three cooperatives

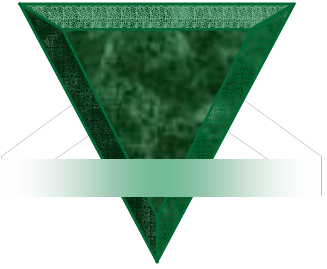


- ✓ 1. Compare the SWOT analysis of Alton Valley with the SWOT analysis of Northstar Ag.
 - Identify the advantages and disadvantages of a merger with Sedgewick Farmers.

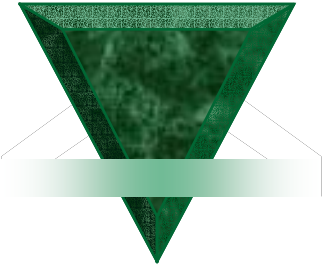
2. Compare the SWOT analysis of Alton Valley with the SWOT analysis of Sedgewick Farmers.
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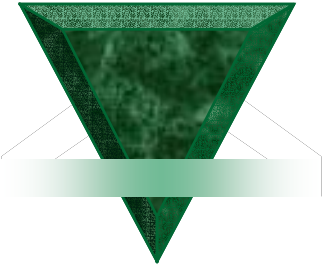
- ✔ Next attempt to identify which of two cooperatives is a better fit with Alton Valley.
- ✔ To help facilitate this analysis is to have students rank the importance of the SWOT once they are all listed.
 - They could next rank items that are “make or break” deal makers on a scale of 1-3.



- ✓ Students should be encouraged to perform or discuss any quantitative issues in their decision-making process.
 - How does the financial analysis fit in the strategic decision?
 - If the class has not used Part A of the case, they shouldn't be precluded from doing financial analysis if the instructor so desires because all of the tables could still be provided to the students.



- ✔ Compare votes between the two cases:
 - If different mergers are selected after each different case, discuss short versus long-term decisions.



- ✓ For director training, discuss two additional questions once the vote has taken place.
 - How would their members view the same issues— would they rank them in the same way as the directors?
 - If not, how would the directors “sell” their decision to their members?
 - This is an important concern facing directors for without a unified front and an understanding of the concerns of their members, a merger could be blocked.