

# FARMERS COOPERATIVE ASSOCIATION

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## General Manager Highlights

By Harlan Schafer

### Fiscal Year 2009 is in the Books

On August 31, your cooperative closed the books on the 2009 Fiscal Year. Since January we've been talking about the challenges that were being faced by the entire agricultural industry, especially those related to fertilizer prices. Most of what I'm about to tell you isn't news; but I think it's worth a recap of events that set the stage for what we now call "last year".

Early in the spring of 2008 Farmers Cooperative was working hard to improve its services, programs and prices to build value and profitability for our producer patrons. Fertilizer prices appeared to be at normal seasonal lows for the 2009 planting season and we began the process of layering in product to have available for your needs. Some of that we sold right away to pass along the apparent low price to those that wanted to prepay, other product was inventoried.

As the summer of 2008 progressed, all fertilizer and fuel prices rose sharply amid news of projected shortages and rising commodity prices. Earlier contracts, both in and out, looked good as grain and fertilizer prices rose to record levels. When Fiscal Year 2008 ended in August, we reported solid savings returning \$800,000 in patronage. We had only started to notice a slight decline in the prices of commodities. By December, it was clear the bottom was falling out of the markets as the entire U.S. and world economy rebounded massively from earlier gains.

At the January meeting of the board of directors, I reported the first of what would come to be many fertilizer inventory devaluations. At that point, all we could do was work through the year, but I remained committed to accurate

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### Fiscal Year 2009 (Continued)

accounting of our financial position through this highly volatile business environment.

Then, as the 2009 growing season unfolded, another key business unit, fuel, was affected by frequent and timely rains that reduced the need for irrigation. We, at Farmers Cooperative, don't complain about rain; rain is free irrigation that adds to your profit; we welcome any advantage for our growers. But many of the contracts we owned to hedge fuel sold under contract to producers were coming off in the spring and early summer with losses of up to one dollar a gallon! Normally that hedge loss would be returned when the contracted fuel is sold. But as producers used less fuel, many of your contracted gallons expired unused in August, at the highest price in eight months. Those returned only sixty cents per gallon to the cooperative.

The dust has settled now and your Board of Directors has reviewed the audited financial statements that showed Farmers Cooperative posted a \$467,000 loss for fiscal year 2009. While those results are extremely disappointing, they are not disastrous. Your cooperative is strong and on stable financial footing. Many "lessons learned" have left us better prepared for business in this new volatile environment. For more on that, please read on.

## How does FY-2009 affect my equity?

I've always considered that one of my main responsibilities to you is to protect and grow your equity in Farmers Cooperative. While our primary focus is to help you be more profitable in your farming operations, we do aim to return a profit for our patron-stockholders.

Unlike private investor-owned companies, agricultural cooperatives typically operate on very thin margins and then, if we make any money, we give most of it back. That has certainly been the case for Farmers Cooperative, returning over 85% of all profits to owners in the form of cash or qualified member equity.

Unfortunately, that leaves very little for the cooperative to reinvest in capital improvements or to absorb the occasional "bad year" without affecting member equity. The last impairment of member equity or "write-down" came in 2002 after the failure of Farmland Industries forced Farmers Cooperative to write \$731,000 in investment equity off of its balance sheet.

After reviewing the results of Fiscal year 2009, however, the Board of Directors has approved taking the resultant loss from Retained Savings, NOT from Member Equity. Obviously there will be no patronage this year, but the good news is that equity balances you've built up will NOT be reduced as a result of 2009 performance. The Company is also in great shape to bounce back quickly from this setback.

Our financial strength was tested in 2009; we've come through a storm unlike anything the industry or our country has seen for over 50 years. I'm pleased to report we are still afloat and the ship is seaworthy. We've implemented several new risk management strategies to help guide us through what promises to be continued volatility in the markets. Crop year and Fiscal Year 2010 look more promising than ever. We look forward to being a part of YOUR continued success and having you be a part of OURS! We'll earn it.

## Pole Line Agronomy Service Center

No discussion of Fiscal Year 2009 would be complete without mentioning our new Pole Line Agronomy Service Center. So far in my discussion of 2009 results I haven't mentioned Pole Line. That's because Pole Line did not cause or significantly contribute to the poor results of 2009. In fact, the 2009 results would have been essentially the same had we done nothing with a new plant. But, and this is important to understand, Farmers Cooperative is in better shape to move forward WITH Pole Line than we would have been without it.

For the past several years, we've been renting storage space in Hastings for much of our annual liquid fertilizer needs. Without storage space, our options to purchase are limited to spring-delivered tons only. That rented space was costing over \$70,000 per year. With the new plant, that payment now goes to investments in assets for this company, not someone else's company. We believe the importance of liquid fertilizer storage space will continue to grow as Anhydrous Ammonia is slowly phased out due to transportation and storage restrictions and cost. And along with liquid fertilizer comes the need to be closer to the plant. Finally, Pole Line gives Farmers Cooperative the ability for contingency planning should something happen to our main plant when you need it and us the most!

All of these factors are as legitimate today as they were a year ago, and maybe more so. Your cooperative now has the ability to do more through the Ravenna plant and the ability to grow at both plants! Yes, we have debt to service, but it's nearly impossible to grow without taking on some long-term debt for the right reasons. Response to the new plant has been very favorable. It came on line in April and performed without a hitch in its first season. It helped relieve pressure at Ravenna and made that plant more accessible for our patrons as well as our operations.

You should be quite proud of the facilities and equipment of Farmers Cooperative; the future is taking shape right now and it LOOKS GOOD!

***Farmers Cooperative, Grow With Us.***

## Market News

So what's going on in the markets?

Fuels have been trending up steadily the last few weeks. Analysts point at recovering world economies creating renewed demand, or the weakening of the dollar with respect to the Euro (oil prices do seem to be a mirror image of the Dollars' relationship to the Euro).

For next spring and summer, farm fuel is currently running about \$2.75 and trending slowly upward. History tells us there may be a "correction" in the November-February time frame, but much will depend on the recovering strength of the U.S. Dollar amid increasing national debt and the potential for inflation.

We are able to make Max-Price contracts that cap your fuel expenses with full down-side opportunity. Talk with Steve Strate or myself for more details on this daily market.

Fertilizer prices have been relatively firm. Dry fertilizer has been softening slightly amid slow demand both in the U.S. and globally. Liquid fertilizers are firming up due to global demand. However, slow demand domestically due to a late harvest and low domestic inventories may be setting us up for much higher prices when product starts moving in the U.S. Early prepays appear to have been a good value, but no fertilizer price is a good price unless it is part of making your operation profitable. Phil and the agronomy sales team review "break-even" prices for your crops on a regular basis. Our objective is less about selling fertilizer than it is about finding ways to make your operation more profitable. That includes finding the best combination of fertilizer and crop protection programs to improve your yield and that work with your grain marketing projections.

You can rely on Farmers Cooperative to be on YOUR side. Count on us to care about what YOU care about and continuously look for ways to improve our service!

## Be Careful with Rumors

With the events of last year and with the way our entire industry was affected, it comes as no surprise that rumors are running wild. I encourage you to be extremely skeptical of rumors, regardless of the source or the subject (us, our competitors, or market partners).

I've spoken directly with area managers from other companies; although most express they were affected to some degree by the market slide of 2008, I have not heard of anyone that is in dire straits.

Most fertilizer companies took some sort of hit; a few did quite well. Most of those companies with grain elevators did better overall than most of the companies without. Every company I've talked to learned something about risk management and every banker has become more educated and involved in the ag-retail business as a whole.

Here's what I can tell you about Farmers Cooperative. While we have, in the normal course of business, discussed mergers; we are not in the process of merging or seeking a merger prospect. Farmers Cooperative is not about to be sold, go broke, or lose supplier relationships. Your cooperative is in excellent position to meet your needs.

In the last year I've been involved in a gut-check that took me all the way to the foundations of this cooperative. I've seen the footings and I found them to be solid. Now we look up.

Let's Grow.

### Mark Your Calendars

**Daylight Savings Time ends November 1**

**Farmers Cooperative will be Closed on Thursday  
November 26<sup>th</sup> for THANKSGIVING**

**2010 Annual Meeting – January 11, 2009**

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## Exclusive General Managers Report

### What Does Your Cooperative Mean to You?

*By Harlan Schafer*

There are those that say the cooperative business model is outdated and obsolete. Why then, I wonder, do we see an almost constant effort to repeal the Capper-Volstead Act of 1922 that gives cooperatives much of their legal ability to work for you, the producer-patron? Cooperatives, at least those that adhere to their genuine and original purpose, always work to bring real market clout to their stockholders in the purchase of inputs and the marketing of your harvest. The day they stop doing that, they're really no different than any privately held supplier or buyer. So how do you know if your cooperative is working for you or if they've fallen into the trap of "thinking like the corporate big-dogs".

- If your cooperative is always "in the market" but the competition is sometimes cheaper, your cooperative is working for you. If the cooperative weren't there, what incentive would the other guy have for trying to "sweeten the deal"?
- Does your cooperative bring you innovative products and practices to help you grow more and profit more, even if it means they may sell less and profit less?
- Does your cooperative work, on your behalf, to create a significant market presence?
- Is your cooperative still your cooperative? Do you know your board members and do you have easy access to senior management staff?

Do you see those things happening in your cooperative?

- I think you'll agree that Farmers Cooperative is always in the market. The other guy can always cut prices, we aim to give you our BEST price the FIRST time.
- I am very proud of new products like SRN 28, Avail, Nutrasphere and Wolfrax that are producing excellent field results as well as our constant efforts to improve operations and application techniques that deliver value to you.
- In 2007, Farmers Cooperative entered the grain business for the sole purpose of getting producers closer to our local processor; now dozens of producers regularly realize thousands of dollars in extra profit they might otherwise never have seen.
- The Farmers Cooperative board of directors recently restated their commitment to remaining an independent local cooperative.

You be the judge; What does your cooperative mean to you?