Is a national pork marketing cooperative viable? A case study of Pork America within the context of structural change in the US pork industry

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Abstract

After World War II, livestock slaughter decentralized and livestock producers increased direct sales to packers. As a result, livestock producers have been less likely than other agricultural producers to use cooperatives to market their farm production. Between 1994 and 1998, less than 15 percent of livestock and wool production was marketed through cooperatives compared with 80 percent of milk production and 40 to 50 percent of grains and oilseeds. Recent structural change in the livestock and meat industries, however, has renewed interest in marketing cooperatives among livestock producers.

In December 1998, the imbalance between market-ready hog supplies and slaughter capacity pushed hog prices to as low as $8 per hundredweight on a live-weight basis. In the wake of these market conditions, the National Pork Producers Council (NPPC) formed a Cooperative Task Force to study the potential for a national pork marketing cooperative. The activities of this Task Force lead to the formation of Pork America.

Pork America is registered in 20 states and its members represent approximately 10 percent of U.S. hog production. The cooperative's goal is to create a producer-owned and controlled pork production, packing and processing system that will provide increased returns to independent producer members. Pork America is currently in the process of developing business and governance structures and identifying pork processing and marketing opportunities.

The formation of Pork America is unique in the history of livestock cooperatives. To the best of our knowledge, it is the first livestock-marketing cooperative that has been organized with a direct nation-wide membership base. In the early part of the 20th century, Saprio fostered fruit, vegetable and specialty cooperatives with a national marketing scope, however production requirements limited membership scope to local or regional production areas. In the 1920s, Saprio's national concept was extended to cotton, tobacco and grain cooperatives, but these efforts collapsed during the depression.

Since the 1930s, the scope of most marketing cooperatives has been generally limited to a local or regional membership base. Those cooperatives that have achieved national membership and marketing scale have done so through mergers and acquisitions. As a result, Pork America has had limited resources of experience to draw on.

A single-case descriptive case study approach will be used to demonstrate that formation of a pork marketing cooperative with a national membership and marketing scope is a viable alternative to merging local and regional cooperatives to realize the economies of size and scope necessary to compete in the pork industry. The method is appropriate because the industrial environment in which Pork America formed contains qualitative and phenomenal information that can not be clearly separated from the quantitative description of industry structure. The single-case approach is appropriate, because as stated above, Pork America is a unique case of cooperative formation.

The case study chronologically describes the formation of Pork America within the context of historical, current, and expected pork industry structure and market conditions. The structural and market conditions demonstrate why the national scope of Pork America is both a viable and desirable achievement. At this point in time, Pork America has not begun operations. Therefore, operational success or failure is unknown. Nonetheless, documentation of Pork America's formation and organizational process is important because of its unique status.

Viability of a National Pork Cooperative: The Case of Pork America

Introduction

Historically, livestock producers, and most especially pork producers, have been less likely than other agricultural producers to use cooperatives to market their products. Nevertheless, attitudes are changing. Spurred by rapid structural change, unfavorable market conditions, and the success of other new generation cooperatives, such as Dakota Pasta Growers and US Premium Beef, pork producers have reconsidered cooperative marketing. In response to the hog market collapse in December 1998, the National Pork Producers Council (NPPC) formed a Cooperative Task Force to study the viability of a national pork cooperative. The Task Force first met in August 1999, and after several meetings, concluded that independent hog producers needed to be directly involved in downstream market stages to avoid being marginalized in the restructuring pork industry. In November, the Task Force presented their conclusions to producers who unanimously voted to form a steering committee. In December, Pork America was incorporated.

Marketing cooperatives that have achieved a national membership base have typically done so through federation, merger or acquisition. In the livestock industry, for example, the National Livestock Producers Association (NLPA) is a federation of regional livestock marketing cooperatives. Farmland Foods, a division of Farmland Industries, has a national marketing presence that grew from a regional base. Nonetheless, Farmland's pork producer members are primarily located in traditional Midwest production areas. Pork America, therefore, offers a unique opportunity to study the development of a cooperative formed with a national membership base.

The study first identifies, from an historical perspective, various measures or criteria against which the viability of this national cooperative model can be judged. A descriptive case study approach is used to apply these criteria to the formation and development of Pork America. Fulfillment of these criteria, as applied to Pork America, is used to demonstrate that this national cooperative model is capable of success. It is therefore a viable alternative to merging or federating local and regional cooperatives to achieve economies of size, scale, and scope. Pork America has not begun operations, so consequently, the study can not address the success of the venture. Nonetheless, the study supports the hypothesis that developing a national cooperative with a direct membership base is viable.

Case Study Methodology

This study contributes knowledge concerning the viability of a specific cooperative model by identifying and describing meaningful characteristics and the interaction of complex economic and social phenomena that affected the formation of Pork America. Yin (1994, p. 1) indicates that case study is preferred when investigators have little control over events and the focus is on a contemporary phenomenon in a real life context. He also stated that the method was appropriate when the topic was broadly defined, when contextual conditions are covered, and when multiple sources of evidence are relied upon (Yin, 1993, p. xi). Sterns et al. (p. 6) support the use of an outlier firm in agriculture and agribusiness case study research:

> When the purpose of the research is to build new theory, two types of case studies could be considered. One alternative is to choose one or two "arch-typical" firms that appear to represent a particular type of firm or decision set. The other option could be case studies made of "outlier" firms that are unique in their standard operating procedures, the business choices they are making, or some other set of distinguishing characteristics of the decision maker and/or firm. Either because they are arch-typical or because of their uniqueness, insights into their success may provide opportunities to broaden the theory base on which to build an understanding of firms and their decision making processes.

In keeping with what Sterns et al. (p. 6) called the "pluralistic epistemology" of the case study approach, multiple types of information have been used. Participants' knowledge, beliefs, perceptions, and values represent their human capital, which describes positivistic knowledge. The Task Force used research, learning and discussion to develop a common understanding about the good and bad prospects for independent pork producers, which represents normative knowledge. The conclusion, that a national cooperative was viable and should be formed, represents prescriptive knowledge that producers should benefit and pay the costs of developing a national cooperative.

The first section of the paper describes the historical evolution of marketing cooperatives in general, and of livestock cooperatives in particular, and is used to identify criteria by which to judge the viability of this national cooperative model. The second section sets the context by discussing the structural change in the U.S. pork industry that motivated the formation of Pork America. Section 3 describes the participants and the processes that the NPPC Task Force used to develop their own criteria and conclude that a national pork cooperative was viable. Section 4 describes Pork America to show that the identified criteria have been achieved. A summary section draws conclusions and proposes further investigation.

Early cooperation

In a 1940 history of marketing cooperatives, Donald Blankerz (Indiana University School of Business) described U.S. farmers' earliest cooperative efforts as haphazard and isolated. He stated that (p. 80) "…no cooperative 'movement' existed, only a series of economic skirmishes against the existing competitive system, a haphazard, sometimes misguided, group of experiments with the idea of cooperation." However, beginning in the late 19th and continuing into the early 20th century, the Grange, the American Farm Bureau, and other general farm associations organized local farmers' marketing and purchasing associations. It was estimated that more than 26,000 such associations were formed between 1863 and 1939 (RBS, 1998, p. 1). In 1929-30, USDA counted a peak of 10,546 farmer marketing cooperatives. This number declined to 6,922 by 1949-50 (RBS, 1998, p. 8).

Many of these early associations offered livestock shipping services, and in 1929-30, nearly 2,200 were classified as livestock marketing cooperatives. This number, however, declined to 580 by 1949-50 (RBS, 1998, p. 15). Despite this decline in numbers, both membership and business volume increased. Membership increased from about 400,000 to more than 900,000 and business volume increased from about $300 million to nearly $1.3 billion between 1930 and 1950 (RBS, 1998, p. 15). Nonetheless, the long-term use of livestock cooperatives has been limited.

Some early cooperative leaders considered a unifying purpose as an essential element to encourage cooperation among farmers. Many early associations, however, mixed purposes, including political, social, and legislative objectives, with business objectives. In 1913, G. Harold Powell, then general manager of the California Fruit Growers Exchange (CFGE was the forerunner of Sunkist Growers), discussed the reasons why many of these associations failed:

> It is generally true that the so-called farmers' business organizations have not been formed primarily to improve the industrial relations of the farmer. They have usually combined political questions, social and legislative problems and business enterprise. Many of them have been formed by impractical enthusiasts with high motives but little business experience, …to found the organization on enthusiasm, altruism, and general discontent. It is a common fault that they have been aimed too high to be useful (Powell, p. 15-16).

In 1915, the newly appointed California Market Director asked Aaron Sapiro to assist him in organizing the state's farmers into cooperative associations. Sapiro borrowed freely from the legal documents of existing cooperatives (including the CFGE, which had been incorporated in

1893). By 1919, Sapiro had developed a cooperative model that was called the “Sapiro plan” (Larson, p. 446-454).

While many early associations were organized geographically, Sapiro promoted organization around a common crop. He believed that cooperatives should consist entirely of farmers and that the cooperative should focus strictly on business objectives. He advocated the use of supply control, which he believed could be implemented through long-term enforceable contracts. Sapiro was an early advocate of pooling and grading, emphasizing consumer benefits gained through information: "[W]hen you grade a product so, for example, that the consumer can get exactly what he wants and does not have to take with it a lot of junk that he does not want, you are increasing the value of the product to the consumer" (Sapiro, p. 22). Many of Sapiro’s concepts have been incorporated into today’s new generation cooperatives.

Nonetheless, by 1926, many of the associations that Sapiro had helped form had ceased to function. Sapiro believed that these associations failed because they did not follow his principles. In 1925, he commented “…that organizing cooperatives was not easy and there was no fixed plan for them. The types of farmers and commodities involved as well as local conditions had to be studied” (Larson, p. 453). Larson, however, concluded that Sapiro’s plan had several defects. Sapiro assumed that cooperatives would operate smoothly if left in expert hands as he moved on to organize the next group of producers. Conflicts developed when Sapiro ignored or opposed existing organizations. He underestimated the complexity of administering large-scale organizations and oversimplified marketing. Finally, Larson concluded that Sapiro did not understand membership relations and overestimated the ability of “ironclad” contracts to guarantee loyalty and maintain enthusiasm among producers (Larson, p. 453).

In 1931, Nourse and Knapp evaluated early cooperative efforts among livestock producers. They identified four major phases in the cooperative livestock marketing movement: (1) formation of livestock shipping associations; (2) formation of cooperative terminal-market sales agencies; (3) formation of cooperative direct-marketing agencies, and (4) the attempt to organize a national livestock marketing association.

The formation of livestock shipping associations was stimulated by railroad expansion, the accompanying growth of terminal livestock markets, and the inability of smaller producers to ship carload lots. The number of shipping associations increased rapidly between 1900 and

1920. By 1923, USDA researchers estimated that 4,000 to 5,000 local associations offered livestock shipping services (Doty, et al., 1926, p. 2). Nourse and Knapp estimated that at least 25 percent of Iowa's hogs were marketed through shipping associations in the 1920s (p. 21). After 1930, however, these numbers decreased as smaller associations were consolidated or ceased operations. Nevertheless, shipping associations were a major factor in the reduction of marketing margins, increased local demand, and provided essential market information. Their successes provided the foundation for the establishment of cooperative terminal-market sales agencies.

The Nebraska Farmers Union is recognized as having established the first successful cooperative sales agency in 1917. In 1920, the American Farm Bureau Federation sponsored the formation of the National Livestock Producers Association (NLPA). NLPA established eleven cooperative commission sales agencies between 1920 and 1923. By 1938, 60 cooperatively owned commission sales agencies handled more than 12 million livestock annually. However, as truck transportation improved and the slaughter industry decentralized, producers increased the use of direct marketing.

In response, cooperatives were organized to assemble livestock for direct shipment to packers, bypassing terminal markets. These direct marketing associations took several forms and some evolved from the consolidation of local shipping associations. To facilitate their operations, direct marketing cooperatives advocated standardization of livestock grades nationwide. Despite cooperative direct marketing activities, cooperatives continued to lose hog market share.

Nourse and Knapp (1931) identified the Federal Farm Board's efforts to establish a national livestock marketing organization as the fourth, and at the time of their review, an unfinished phase in the development of a cooperative livestock marketing industry. While Nourse and Knapp believed that the Farm Board's efforts had sound economic foundations, they perceptively identified factors that would, eventually lead to the failure of the National Livestock Marketing Association's (NLMA) efforts to develop a truly national livestock marketing cooperative.

Nourse and Knapp concluded that the Farm Board had allowed political expediency to overrule co-operative doctrine. Consequently, the development of the NLMA proceeded along

promotional rather than cooperative lines. In addition, they stated that the Farm Board was intolerant of other cooperative endeavors among livestock producers. The net result was the lack of a properly constituted underlying organization of producers (p. 345-366). They summarized organizational efforts of the Farm Board thusly:

> They are, of course, mutualized corporations in the sense that residual benefits go to the member patrons and not to stockholders. The patron member, however, has so remote a contact with the organization and so little of a sense of participation in its management that the essential character of the co-operative association is almost completely lacking. This means, on the one hand, that his continued adhesion to the organization must be based largely upon measurable (and rather immediate) pecuniary benefits and not upon belief in the value of long-time results to be accomplished through group organization and loyalty to such constructive programs as he himself has helped to formulate. On the other hand, it means that the potential savings which co-operation proposes to make by utilizing the voluntary and gratuitous participation of its members will to a greater or less extent have to be dissipated in promotional work. This is the major one of the "wastes of competitive capitalistic business" which the co-operative is supposed to avoid. (p. 349-350)

The use of centralized public stockyards diminished as hog packers continued to procure increasingly more hogs directly from producers. By 1972, only 30 percent of hogs were marketed through public markets (Packers and Stockyards Programs, 1996), decreasing to less than 4 percent by 1997 (Packers and Stockyards Programs, 1998). Consequently, livestock marketing cooperatives continued to lose market share as hog producers sold directly to packers through networks of packer-owned buying stations and exclusive buying agents. In the 1990s, regional livestock marketing cooperatives that were primarily NLPA members, marketed less than five percent of the hogs slaughtered, representing 3 to 4 million head annually.

Cooperative livestock shipping associations, terminal-market sales agencies, and direct market sales agencies where successful at various times, but early attempts to form cooperative slaughter businesses nearly always met with failure. R.L. Fox reviewed these efforts in 1957. The first recorded cooperative meatpacking endeavor took place in La Crosse, Wisconsin, in 1914. Twelve other attempts would be made between 1914 and 1920. Of these efforts, only one lasted more than 3 years, and with one exception, all had ceased to operate by 1923. Producer interest in cooperative slaughter and meatpacking remained dormant until 1930. Thirteen cooperative slaughter and meat processing businesses were started between 1930 and 1948; eight failed by 1950; six had operated less than a year. Fox (1957) identified insufficient capitalization; lack of producer commitment; inadequate marketing operations; and inadequate management as contributing factors in the demise of these cooperatives.

Despite these failures, cooperatives have had commercial successes in the livestock processing industry. Most prominently, Farmland Industries entered the pork processing industry in 1959. Farmland is today the sixth largest hog slaughter in the U.S. Farmland is an open membership cooperative, and therefore, primarily purchases hogs on the open market. Nonetheless, 70 percent of the hogs Farmland processed in 1999 were purchased from members (Securities and Exchange Commission). Farmland currently operates slightly more than 6 percent of U.S. daily hog slaughter capacity.[1]

The early success of cooperative livestock shipping associations and cooperative terminal-market sales agencies did not translate into the same level of success in direct marketing cooperatives or livestock slaughter and meat packing cooperatives. Nourse might claim that this was the inevitable result of the shipping associations and terminal-market sales agencies successfully performing their competitive yardstick function. By making livestock markets and investor-owned livestock processing firms more efficient, farmers were able to reallocate their resources to production activities, and thus, their cooperatives exited the industry.

The long-term effect, however, appears to have left hog producers in a more precarious market position as the pork industry consolidated and restructured than they might have been had they sustained the cooperative hog industry at earlier levels. The dairy industry offers a contrasting example. Dairy producers have been committed to the use of marketing cooperatives for more that a century, and market more than 80 percent of their production through cooperatives. Consequently, they have been able to leverage cooperative equity into a significant position in a restructured dairy industry.

Structural change in the 1990s – Motivation for cooperative innovation

In the 1990s, independent hog producers faced increasing horizontal concentration and vertical coordination that has been characterized as the industrialization of agriculture. As the volume of hogs traded via open market transactions has decreased, independent hog producers, family-farm organizations, and elected officials have questioned both the hog marketing system's integrity and its ability to offer a competitive price. Many producers believe that these changing structural conditions have limited their access to competitive markets.

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[1] Calculated from estimated daily slaughter capacity data in "Pork Facts, 2000/2001," National Pork Producers Council, Des Moines, Iowa, p. 25. Prior to the sale of the Dubuque, Iowa facility, Farmland's share of daily capacity approached 9 percent.

Horizontal concentration at the producer level has been documented in USDA's Hog and Pigs reports. In 1988, operations with less than 1,000 hogs accounted for 96.8 percent of hog operations and 63.9 percent of U.S. hog inventories (Agricultural Statistics Board, 1994). In 1999, operations with less than 1,000 hogs still accounted for the overwhelming majority of operations, 86.2 percent. However, these operations accounted for only 18.5 percent of inventories. Meanwhile, operations with 10,000 or more head accounted for only 2 percent of operations but possessed 46.5 percent of inventories (Agricultural Statistics Board, 1999).

Freese (1994, 1999) has documented horizontal concentration among the largest U.S. hog producers. In 1994, the 31 largest U.S. pork producers ranged in size from 10,000 to 180,000 sows. These operations owned 1.1 million sows that represented 16 percent of the U.S. breeding herd. In 1999, the top 50 producers ranged in size from 7,200 to 785,000 sows. These firms owned more than 2.6 million sows that represented nearly 42 percent of the U.S. breeding herd. The top four firms owned 481,800 sows, 6.8 percent of the breeding herd, in 1994 compared with 1,092,0002 sows, 19.4 percent of the breeding herd, in 1999.

Pork supply chains, vertically aligned systems designed to coordinate production from the genetic base to retail customer, are emerging as the industry model. Investor-owned firms, including Smithfield Foods, Seaboard Corporation and the Contigroup Companies (Premium Standard Farms), have implemented a supply chain strategy through ownership. Freese (1999) reported that packers with vertically integrated production operations owned more than 1.3 million sows in 1999 compared with less than 220,000 sows five years earlier. With the acquisition of Murphy Family Farms in January 2000, Smithfield Foods estimates that their vertically integrated production operations supplied 60 percent of the their U.S. hog slaughter capacity. Recent estimates suggest that, industry wide, vertical integration accounts for 15 (Hayenga et al, 2000) to 24 (Grimes and Meyer, 2000) percent of production. Other investor-owned packers and processors have implemented supply chain strategies through long-term marketing agreements. Grimes and Meyer (2000) reported that 73 percent of hogs procured by the 13 largest packers in January 2000 were obtained through some form of marketing agreement, up from a similar estimate of 57 percent in 1997.

[2] The four largest firms were Smithfield Foods/Murphy Farms, ContiGroup, Seaboard, and Tyson's based on the termination of Smithfield's plans to purchase of Tyson's production units.

Paarlberg et al. (2000) believe that these structural conditions have the potential to limit market access. They stated: “The development of tighter linkages in the food production and distribution industries may have a major impact on market access in both the input and product markets.” They went on to state that "…cooperation and pooled production and marketing appear to be key to offsetting the impacts of consolidation and integration in today's pork industry." Nevertheless, they recognized that “…the livestock producing community has little experience and expertise in using these alternatives and will likely need public policies and assistance to get them functioning.” Cook went further and said that cooperatives can provide a device for farmers to network with the rest of the supply chain and that consolidation can actually open doors for entrepreneurs using cooperative relationships (AgWeb.com).

The effects of structural change were highlighted in December 1998 when the supply of market-ready slaughter hogs collided with available slaughter capacity. Many producers found their access to markets impaired. USDA Market News (1999) reported live-weight equivalent prices as low as $8 per cwt., the lowest in nearly 50 years. Producers’ share of the retail value of pork dropped from 33 percent in July to 12 percent in December 1998 (Duewer).

Renewed interest in cooperative marketing among hog producers has been especially keen for new generation cooperatives. However, new generation cooperatives are based on significant up-front investment of producer equity as opposed to equity retained over time in traditional cooperatives. Unfortunately, the ability of hog producers to generate up-front equity capital has been limited by more than two years of farm-level equity loses. Ron Plain (2000) estimated that the hog production sector lost $4.4 billion in equity between November 1997 and March 2000. The wreckage left in the wake of structural change and market failure motivated pork industry leaders to investigate the formation of a national pork marketing cooperative.

NPPC Initiative and Task Force

In April 1999, NPPC officials presented the idea for a national pork producer cooperative to Cooperative Service personnel and requested technical assistance to investigate this concept. The concept initially focused on expansion of slaughter capacity. This focus was motivated by the conclusion that low prices were primarily driven by a misalignment of incentives. Producers had expanded hog production capacity in response to demand growth. Whereas, packers had closed hog slaughter capacity that was costly to maintain when cyclical and seasonal low hog numbers made it difficult to operate plants efficiently.

To alleviate this imbalance, the NPPC proposed that a national cooperative would build three state-of-the-art plants of sufficient size to be competitive given the economies of the pork slaughter industry. This implied large-scale plants that would require large networks of producers to supply. In this model, operational efficiency and profitability would have been dependent on factors that were, at that time, unknown and beyond control. These included the location and concentration of potential members willing and able to invest capital; the competitive response of other market participants; and the willingness of existing local, state, and regional groups to set aside traditional parochial interests to participate in a national endeavor.

The NPPC announced this effort to form a national pork producer cooperative as part of its economic recovery plan and introduced the concept at the 1999 World Pork Expo (Appendix A). As part of this recovery plan, the NPPC estimated that government intervention in the form of equity capital, estimated at $150 million, would be needed to finance the project. A task force would be charged with the responsibility to investigate the viability of a national pork producer cooperative.

The NPPC plan embraced the new generation cooperative concept. Producers would provide up-front investment to capitalize the business through the purchase of delivery rights, which would also define the cooperative's supply. In return, producers would be compensated based on the long-term consumer value of pork rather than short-term hog prices. Transfer pricing would be non-discriminatory, but would include premiums and discounts to reflect cost-related differences in the seasonality of production and delivery mechanisms. Incentives would be developed to spur producers to implement genetic programs and production methods that directly reflected marketable consumer-driven product characteristics. The viability criteria implicit in Sapiro's plan, which have been proven viable through the success of other new generation cooperatives, were, therefore, implicitly addressed.

At this point in the process, however, the plan did not meet criteria implicit in Larson's evaluation of Sapiro associations or Nourse and Knapp's evaluation of the National Livestock Marketing Association. The project was top-down, driven by political expediency, and would require promotional effort to implement. In addition, the concept focused on plants, rather than the producer participation necessary to make the project viable.

To study this plan, the NPPC identified 22 potential Task Force members; 15 persons agreed to serve on the Task Force, and a core group of 9 or 10 individuals emerged as the driving force of the proceedings. Given the urgency to do something, Al Tank, NPPC CEO, commented that Task Force members had been chosen for their drive and impatience. The Task Force members represented a cross section of the pork industry in terms of experience, expertise, and geography.

Most were producers, but other areas of the industry were represented as well, the feed sector, the livestock-marketing sector, and several academicians were included. Producers came from a variety of backgrounds and various sized operations. Both traditional and non-traditional production areas were represented. Some had previous experience with production, supply, or marketing cooperatives; several had served as cooperative board members. Others had no previous experience with cooperatives. Not all of Task Force members' cooperative experiences had been positive. Several members had previously served as NPPC members or served on other NPPC committees.

The Task Force brought together a diverse group that had a broad base of knowledge, a wide range of pork industry experience, and various degrees of cooperative experience. Task Force members had a passionate belief that something needed to be done to help independent producers access markets and continue to be viable industry participants. Nonetheless, this enthusiasm was tempered with skepticism that a national cooperative could be viable.

The Task Force's first objective was to gather sufficient information to provide each member with a common base of knowledge from which to work. The Task Force heard presentations on (1) industry structure and market conditions, (2) cooperative structures and characteristics, and (3) the successful application of the cooperative model in the livestock industry. To focus it's activities, the Task Force defined its mission "[T]o create a national producer owned cooperative that will coordinate pork production, processing, distribution, and marketing to optimize opportunities and profits for the producer members."

Based on this mission and the information gathered, the Task Force defined six criteria that they believed the cooperative must fulfil to be viable from the producers standpoint. The cooperative must be able to:

1. Capture a greater portion of the economic value of pork and return it to producers;
2. Identify and recruit producers willing and able to supply sufficient equity capital and market hogs necessary to make the venture efficient and effective;
3. Develop a system that pulls pork through the marketing chain based on consumer demand rather than pushing pork through based on members' production decisions;
4. Implement solutions to address the imbalance between cyclical and seasonal hog production and slaughter capacity;
5. Offer pork producers opportunities to realign themselves in the pork value chain and maintain their identify as viable independent businesses in the pork industry; and
6. Exploit the "story" of independent U.S. producers to create value in both the domestic and export markets.

These criteria reflected the Task Force's adamancy that the cooperative should focus on business objectives, which should not be compromised for social or political objectives. This single-mindedness fulfilled the Sapiro criterion. The Task Force, however, appeared to reject consideration of intangible social and political objectives as criteria for viability. This, however, did not reconcile with Larson's argument that early Sapiro associations failed for lack of member relations. It also appeared to be inconsistent with Nourse and Knapp's assessment of the NLMA, and Fox's finding the producer loyalty was an essential element of processing cooperative success. It was unclear if the Task Force was rejecting the intangible social and political aspects inherent in any human organization as criteria for viability or just prioritizing.

Cooperatives like all human organizations, are inherently social entities. To effectively perform the cooperative's business functions, cooperatives must foster relationships – a social criterion – among producers as both owners and suppliers, the board of directors, cooperative management, cooperative employees, and customers. These criteria may be even more important in today's knowledge-driven, relationship-based economy. It is important, therefore, that the cooperative is considerate of the implicitly social aspects of governance and operational structures regardless of the business goals or economic objectives that it hopes to achieve. In addition, agricultural producers and processors operate in an especially politicized environment. To conceive that the cooperative could be considered viable without consideration for the political aspects of food production and processing may not be reasonable. Nonetheless, the Task Force's focus was on the financial viability of a national cooperative.

To address financial viability, the Task Force commissioned a study to strategically analyze the viability of a national cooperative in the pork industry. The study concluded that to be viable, a

national cooperative must not only be producer-owned and controlled; it must also be an attractive and profitable investment. Focusing on the cooperative as an attractive and profitable investment, the study concluded that the pork industry met these criteria for the following reasons.

Much of the pork processing industry's infrastructure is aging and obsolete. Some existing plants are poorly located relative to current hog supplies. Investor expectations and long-term goals of the investment community have caused some investor-owned firms to consider strategies to exit the industry. Independent processors without hog slaughter capacity appear to be eager to strategically partner with producer-owned firms to assure themselves of a source of consistent high-quality raw materials. The study estimated that the product from a single hog was valued at $340 at the retail level, and that a portion of this value could be captured through producer-owned vertical integration. These factors, combined with the pork industry's potential for growth, suggested that viable opportunities existed for a national cooperative to enter the industry and return significant benefits to independent pork producers.

After concluding that a national cooperative could be an economically viable entity under certain conditions, the Task Force invited producers and producer representatives to a meeting to gage producer interest. The meeting was held in Des Moines, Iowa in November 1999. It was estimated that the producers represented at the meeting marketed nearly 20 million market hogs annually, or nearly 20 percent of U.S. production. The Task Force presented a summary of the information that they had gathered during the previous four months, and introduced their model for a national cooperative.

The model was characterized as the "Umbrella Model." It envisioned that producers would primarily be direct members of the national cooperative. However, the model also allowed producer groups and other cooperatives to be members. Nonetheless, the model was based on the concept that producer ownership, control, and the opportunity to participate in businesses activities would be enacted through the national cooperative. The model envisioned that various business activities would take place under the umbrella of the national cooperative. The model recognized that business entities could take on various business structures including that of a cooperative, a joint venture, or a limited liability corporation. That is, business structures under the cooperative umbrella would not be predetermined. However, the model did not necessarily imply that the cooperative would own bricks and mortar assets.

Unknown to the Task Force, this model implicitly addressed Nourse and Knapp's complaint that the Farm Board's intolerance of other cooperative efforts negatively affected the viability and success of the NLMA. By encouraging and including all potential opportunities for cooperation among producers, in terms of both potential members and business activities, the Task Force achieved the criteria implicit in Nourse and Knapp's complaint, which further bolstered the potential cooperatives viability.

After participation in focus groups and small group discussions, the group was reconvened to consider the next step. After some discussion, the group unanimously voted to form a steering committee to under take the formation of a cooperative. The steering committee consisted of core Task Force members and several producers that had not participated in the Task Force proceedings. Pork America was incorporated in December 1999.

What is Pork America?

Pork America was officially incorporated under Minnesota cooperative law on December 29, 1999. The founding board consisted of eight members from six states: one each from Illinois, North Carolina, Texas, and Ohio, and two each from Minnesota and Kentucky. All of the founding board members were members of the steering committee and had participated in the NPPC Task Force. Before the board member convened its first meeting, the member from Ohio resigned for personal reasons, and was replaced by a member from Iowa.

The board initially described Pork America as a national umbrella cooperative that would facilitate and coordinate among individual producers, as well as local and regional groups. It would act as a resource center for activities related to the production, delivery, and marketing of hogs. In addition, Pork America would foster research and development activities needed to assure that its members supplied quality products precisely targeted to the needs and wants of consumers and end users. This initial vision held that Pork America would primarily act as a coordinating agent, as opposed to directly owning and operating harvesting and processing plants.

Making use of the strategic market study commissioned by the NPPC Task Force, the Pork America interim board identified two keys to success. First, Pork America must be market driven. It must develop innovative dynamic models to meet market demand; it must penetrate

the market by identifying solid business opportunities; and it must develop structures and systems that facilitate supply chain alignment and producer-to-consumer coordination. Secondly, Pork America must be a significant industry player on a national scale. It must develop the ability to control, participate in, drive and create pork-based food activities on a broad scale and seek to become a top-tier player in the pork and food industry. While these keys to success were consistent with Sapiro criteria, they did not seem to fully address criteria implicit in Larson's, Nourse and Knapp's, or Fox's critiques.

This became evident as Pork America began to solicit membership. The national scope of the project slowed membership recruitment. Pork America was counseled not to sign up members from any specific state until registration in that state had been completed. The challenge of registering in the 20 states that Pork America originally targeted was time consuming. Local and state based groups that did not have to overcome these legal hurdles were forming. One of the board members commented, "We didn't quite realize how difficult it was going to be, to get everything done on a legal basis A national cooperative had never been done like this before. Most of the other national cooperatives had come together as a result of mergers of regional cooperatives. We're starting something really new."

Nonetheless, the Pork America board persevered. When Pork America's Foundation Membership drive closed on June 30, 2000, Pork America had signed up individual and group members from seventeen states. Pork America estimated that these producers and producer groups represented ten million market hogs, or approximately 10 percent of the U.S. total production. These hogs, however, have not been committed to Pork America projects. Foundation membership does include priority to participate in future Pork America projects.

After this initial membership drive, the Pork America board focused on strategic planning, and identifying and developing business opportunities. The board worked with a strategic planning consultant to identify strategies to achieve Pork America's goals:

1. Increase efficiency by improving producer-to-consumer information flow;
2. Coordinate production, processing and marketing through real-time internet-based information management systems;
3. Develop systems and partnerships to sell as close to the retail consumer as possible, including development of an independent producer brand;
4. Avoid head-to-head competition with existing large players by identifying and supplying undeserved segments and niches; and
5. Support new and existing producer groups and return profits to the local level by developing and supporting pork-merchandising opportunities.

To implement these strategies, Pork America hired NPPC past-president John McNutt as Director of Development. This decision varied from what has been the observed first hire of many other new generation cooperatives, a Chief Executive Officer. Pork America's interim board, however, determined that they first needed to identify business opportunities and develop business plans, before they hired a CEO to implement these plans.

Despite a substantial commitment of time and personal resources by Pork America's interim board, some members had grown restless. Tangible results were not evident. In August 2000, the Pork America board invited members to a meeting in Des Moines, Iowa for a progress report. At that meeting, members were able to voice their concerns. The board had these members participate in a planning workshop to provide guidance. Members approved the board's progress to that point, but requested more tangible results of the boards progress in six months.

The board reinforced and focused their efforts to identify specific and credible business opportunities. In this process, they discovered that their original intent to have Pork America act only as a coordinating agent was not viable. To fulfil its objectives, Pork America would have to consider opportunities that involved controlling or owning physical assets. To present identified opportunities to members, an annual meeting was scheduled for November 4 in Kansas City, Missouri. At this meeting, the interim board would put their credibility on the line by, for the first time, standing for election. Members showed their approval of the boards efforts by electing six of the original interim board members to fill seats on the six-member board. This elected board is now moving quickly to develop business plans to implement the business opportunities presented to members at this meeting.

Conclusions

In the process of developing this cooperative, pork producers initially focused on the business and financial criteria implicit in Sapiro's plan. That is, they believed that if the model was shown to be a profitable investment that it would be successful, and therefore they could conclude that the cooperative would be viable. While this may be a necessary condition for viability, it has not appeared to be a sufficient condition from an historical perspective. This was demonstrated though Larson's critique of Sapiro's associations, Nourse and Knapp's evaluation of early cooperative livestock marketing efforts, and Fox's critique of early cooperative livestock slaughter efforts. Like many efforts before them, pork producers initially failed to consider the

inherent social and political factors that must be overcome before the cooperative can implement its business plans.

Soon after it was formed, however, Pork America's interim board began to learn valuable lessons in member relations, customer relations, community relations, and even competitor relations. They have learned that their business objectives can not be achieved in a social or political vacuum. Consequently, Pork America has identified one of its strengths as its ability to identify industry expertise and develop relationships with other producer groups, customers, and communities. Nonetheless, many potential members have not embraced Pork America's strategic vision, and many producers, including some members, continue to sit on the fence, unwilling to risk resources to support Pork America's developmental efforts.

From our observations of Pork America's development and growth, we conclude that development of a cooperative based on direct participation of a national membership base is viable. Nonetheless, it appears that the bar for success is much higher. While Pork America is based on the concept of direct producer participation at a national level, the viability of Pork America appears to require the participation of local and regional groups as well.

Continued concentration and structural change in agricultural processing, food manufacturing, and food retailing industries suggests that, to some extent, and in many cases, size matters. The ability of relatively small agricultural producers to participate in these industries as strategic partners as opposed to cost centers may be dependent upon their ability to develop and maintain cooperative enterprises on a wide geographic basis. Continued documentation of the development of Pork America can offer unique insight into how pork producers handle this process, and may influence whether other producers groups may want to attempt to form cooperatives on this scale in the future.

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Appendix A

The Concept of a National Pork Producers Cooperative
As announced at the 1999 World Pork Expo

Over the past 24 months the U.S. pork industry has lost approximately 8 percent of its daily slaughter capacity or approximately 37,000 head of shackle space. This shackle space crisis manifested itself in the fall of 1998, when production exceeded slaughter capacity, creating massive bottlenecks at the back door of packing plants and plunging market prices to the lowest levels since the Depression. What began as a shackle space crisis, quickly spawned a liquidity crisis for producers and culminated in a business crisis for the pork industry. Today, it is clear that additional slaughter capacity will be lost in the next 24 months as old or inefficient packing plant(s) are closed. At the same time, the producers share of the consumer dollar spent on pork fell to a record low of 26 percent in 1998 (including an all-time monthly low of 12 percent in December 1998), despite record values in the pork chain. It is imperative to create a vehicle by which pork producers can have access to adequate shackle space, while positioning themselves to capture value in the pork chain. The time is right and the need is clear for the creation of a national pork producers cooperative, which builds, owns and controls state-of-the-art-packing plants, thereby repositioning producers in the supply chain.

Independent producers from many areas have been discussing the formation of cooperatives or other business structures to slaughter and process hogs. However, the size of many of these proposed operations would place them at a cost disadvantage when compared with existing investor-owned packing plants. Therefore, a cooperative that is national in scope and commitment is needed

At the present time, a number of producer-owned cooperatives have successfully positioned producers in the value chain of other sectors. Some examples include: Ocean Spray, Goldkist (the second largest broiler producer and processor in the U.S.), Sunkist and most notably, Danske Slagterier, the Danish pork producer cooperative that owns and controls all of the slaughter capacity in Denmark. It is our intention to create a national pork producer cooperative utilizing the successful components of these and other successful supply-chain, marketing cooperatives. As a result, this national pork producer cooperative would directly address many of the major challenges facing pork producers, including: increasing shackle space, increasing competition, reducing concentration while allowing producers to reposition themselves in the pork chain.

Functions
The cooperative would slaughter, process, and market fresh pork and further-processed pork and pork products on behalf of its independent member producers. To enhance the value added by processing and strengthen net returns to hog producers, the cooperative would most likely need to establish a branded presence in the marketplace or work directly with pre-established end-users.

Structural Form and Governance
The cooperative would be structured as a new generation value-added cooperative with a target membership of independent U.S. pork producers. Producers have not limited themselves to sole proprietorships, therefore, a definition of independent producers for general membership purposes would be developed. Producer equity would be raised through the sale of two types of membership shares: general membership shares and a second class linked to capacity.

Control through voting rights in most traditional cooperatives is based on one-member one-vote, however, a number of successful new generation cooperatives utilize proportional voting. These shares would be transferable to other general membership shareholders.

Operations
The cooperative would build and operate state of the art slaughter and processing plants, designed to achieve optimal operational efficiencies. Therefore, site selection criteria would likely include, but not be limited to: (1) location and concentration of prospective members willing to invest ownership capital; (2) location and concentration of current hog production; (3) location and concentration of current slaughter and processing capacity; (4) location of groups currently organized to consider cooperative opportunities; (5) transportation costs; (6) consumer market access; (7) local support; and (8) labor supplies.

The National Pork Producers Council (NPPC) has initially proposed three plants, but further investigation would be conducted to determine the optimal number and proper locations. As information, the following calculations reflect the potential size and scope of new slaughter capacity being discussed:

8,000 head/day x 3 plants = 24,000 head/day x 5.5 days/week = 132,000 head/week x 52 weeks/year = 6.86 million head/year single shift capacity (note: potential for 13.7 million/year if double shifted)

6,000 head/day x 3 plants = 18,000 head/day x 5.5 days/week = 99,000 head/week x 52 weeks/year = 5.15 million head/year single shift capacity (note: potential for 10.3 million/year if double shifted)

The cooperative could seek to coordinate efforts with other cooperatives to leverage producer owned resources for maximize returns.

Benefits to Producers

The benefits to independent pork producers are to maintain or increase market access, reduce risk, and generate greater net returns.

Rapid structural change in the swine production and slaughter sectors resulted in conditions where market access and prices quickly deteriorated when investor-owned slaughter facilities operated at or near capacity. This was apparent in December, 1998 when market hog prices fell to levels unprecedented since the Depression. This is increasingly evident given the greater inelasticity of demand for live hogs which has been manifested over the last two live hog cycles. Pricing methods based on end user valuation of pork and pork products rather than traditional pricing systems should reduce this risk.

Failure to act is not an acceptable option.

Source: http://www.nppc.org/PROD/coopconcept.html.