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## CONTRACTING IN THE BRITISH AGRICULTURAL SUPPLY INDUSTRY

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Agricultural supplies to farms in the United Kingdom at 1974 spring prices were estimated to be in excess of 2,000,000 pounds (sterling) a year. This sum covers animal feeding stuffs, grain and seed, fuel and fertilizers, agro-chemicals and machinery, as well as miscellaneous items such as baler twine. In addition, the Agricultural Supply Industry procures from U.K. farmers grain for animal feed manufactures and seed for cleaning and treatment worth around 500 million pounds (sterling) so that the total value of the trade between the Agricultural Supply Industry and U.K. farmers is in excess of 2,500 million pounds (sterling) a year.

"Contracting" for the purposes of this paper is defined as the provision of supplies of agricultural requisites against a formal agreement or contract for a period of one year or more. Contracting in this sense is not a general feature of the industry in the U.K., but it is found most frequently in certain sectors of the industry in which there is severe competition for large parcels of business with very low margins per unit. For example, tractor fuel and lubricants, animal feeding stuffs, fertilizers and crop protection chemicals.

To the supplier, contracting makes for orderly marketing and the more efficient organization of distribution of the secured business. To the farmer it can give an assurance of supplies at agreed prices and terms.

The actual terms of agreement vary from one sector of the industry to another, but before describing the practice in my own sector - the fertilizer business - I shall quickly review the industry as a whole so that our own approach to contracting can be seen in the context of the whole industry.

The simplest form of agreement that falls within this definition of "contracting" is probably that employed by the major distributors of fuel oil and lubricants. Their products are in continuous demand and brand differences are small. Hence competition is very severe. In the U.K. the bulk of the trade is held by a few importers and refiners who operate their own direct selling distribution chains. Their excess production is, however, sold to a number of small independent distributors who maintain a cut price operation with minimum overheads.

Contracts for agricultural fuels and lubricants are typically between a major supplier and an individual farmer to supply his total requirement of agricultural fuel or of lubricants for use on his own farm for a minimum period of a year. The agreement then continues in force until terminated by either party giving six months notice. Each agreement specifies the rebates that have been negotiated off the wholesaler's scheduled prices.



With agro-chemicals, contracting is centred on the supply of wide spectrum weedkillers such as MCPA and 2-4D which again are a high volume, but very competitive market in which margins are minimal. Manufacturers strive for this business because it brings with it a demand for other sprays and chemicals. However, contracting is practised only by a minority of agro-chemical manufacturers in the U.K. Together they may have around 20% of the total business but no measure exists of how much of this is subject to any contract arrangements.

In this sector the most common form of agreement relates to the provision of a sprayer by the agro-chemical manufacturer on special discount terms in return for an undertaking by the farmer to purchase a stipulated minimum quantity of spray chemicals over a period of 3 to 5 years. The price of the chemicals does not enter into the contract. In each case the choice of sprayer is very limited. There is often a limit to the number of machines available because they are purchased from the machinery manufacturer on very favourable terms. The spray manufacturer by contracting for business in this way is aiming to secure large parcels of the cut-price weedkiller business with little or no reduction on his list prices. It is evident that suppliers are very selective in their choice of customer for contracts of this kind.

Most of the major agro-chemical suppliers in the U.K. have so far refrained from offering contracts like this, but two nationwide distributors and a number of local merchants are either supplying sprayers on special discount terms or leasing machines with 1 to 3 year options to purchase with the backing of certain Finance Houses. There is also some leasing of sprayers for 3 to 5 year periods to custom operators whose business is thus secured in the same way.

Within the agro-chemical sector contracting has been a recent development and it is really too soon to judge its success because few of these contracts have yet been completed. One can foresee difficulties for the supplier who may be unable to retain the business once the term of the contract has expired if the farmer has been dissatisfied with the machine.

To quote a specific example reported in the Agricultural Press, discount for sprayers of three different models offered in the Shell Chemicals scheme in February 1974 ranged from 75 - 305 pounds (sterling). These discounts were available to any grower or farmer contracting to purchase a minimum quantity of Shell pesticides over the next 3 to 4 years.

As an extension of this form of contracting in the agro-chemical sector we should note the provision of specialist equipment to local contractors or custom operators who are thus obliged to use the manufacturers products. As each contractor may have little competition in his own locality this method of contracting with a custom operator secures the spray chemical business from a greater number of farmers. An example of this can be seen in the development of direct drilling in Britain. By arranging the manufacture and



supply of the special drills required, albeit through the established channels of the farm machinery trade, and by its provision of specialist technical and agronomic advice to contract operators, Plant Protection Limited are securing spray business that extends beyond the supply of the 'Gramoxone' required for the direct drilling service.

Feed manufacturers in the U.K. have concentrated contracting schemes, in the main with poultry and pig feeds. Until the escalation of raw material prices in the past two years the major compounders were offering dairy farmers, in particular, fixed contract prices for feeding stuffs supplies for the winter period. This was usually in two parts from the autumn through to the end of the year and from January onwards.

The farmer was able to plan ahead and the manufacturer was assured of a proportion of the market. In recent years feed manufacturers have followed the example of some of the fertilizer manufacturers and have contracted feed supplies in return for a variety of farm business services. The farmer sometimes pays a fee for the business service and also contracts for a minimum tonnage of feed but he is not tied to price.

The types of contract which are available for pig and poultry feeds have a number of permutations and combinations. At one end they may involve the feed manufacturer in providing the young stock and the feed at his own expense, arranging for the disposal of the fattened stock and paying the farmer a management fee of so much per head. Most contracts are on the whole less restrictive than this and allow some latitude on the choice of feed. In most cases the farmer would be the owner of the stock which will have been purchased from approved suppliers. Perhaps the major contribution which the feedingstuff industry had made during the past decade has been in finding outlets for the livestock producers' finished products and encouraging farmers to produce to the buyer's specification by using standardized basic breeding stock, feed and husbandry techniques. This relationship has benefited both the farmer and feed manufacturer.

With feedingstuff prices increasing by about 100% over the past twelve months the incentive for farmers to contract their feed supplies and so reduce the risk of rapid changes in the cost of a major raw material has increased considerably, especially for pigs and poultry which have a shorter production cycle.

In the fertilizer trade contracting or the use of formal agreements has been a fairly recent development. Here again it can be seen to have started in an attempt by manufacturers to secure business in the face of the intensive price cutting of a few years ago. In each case, in return for an agreement by the farmer to purchase a stated minimum tonnage of fertilizers for a stated period normally not exceeding three years, the manufacturer provides a facility ranging from a fertilizer spreader at an attractive price or a pallet exchange service or a foreloader to sophisticated farm business aids such as 'MASCOT', ICI's linear programming service.



One major manufacturer offers a pallet exchange service tied to a 3 year agreement and a reduced price for the initial stock of pallets while another provides for lift trucks of a well known British make at reduced rates against 3 year fertilizer supply contracts.

It is a feature of the U.K. fertilizer business that the major manufacturers sell their products largely through independent agents. These contract schemes oblige the farmer to buy the manufacturers branded product, but leave him free to purchase it through the agent of his own choice. Thus, the individual farmer remains free to negotiate the best terms that his own business will justify while the manufacturer is assured of an outlet for his product. However, as a further development a number of the largest fertilizer agents have seen an advantage in joint participation with the manufacturer in some of these schemes.

Contracts involving the provision of farm business aids have been pioneered by I.C.I. although it by no means has a monopoly of them. This type of contract is attractive to the farmer, since he is able to obtain free or relatively cheap farm business advice yet at the same time he is free to purchase his fertilizer requirements at the best market price.

I.C.I. DAIRYMAID was launched in 1970 and provides a forecast on a monthly basis for a year and the farmer is able to have his performance monitored. At the moment over 3000 dairy farmers in the U.K. have contracted for this service on an annual basis. It is free in return for the purchase of I.C.I. fertilizer.

Similarly, I.C.I. BEEFMAN monitors the performance of beef cattle on an individual animal or batch basis. Although only introduced recently, over 300 farmers have contracted for the service.

'MASCOT', a computerized farm planning service based on linear programming, has a particular application on a large complex farm, particularly arable. It has been operational since 1969 and each year to date about 100 large commercial farmers have contracted to purchase I.C.I. fertilizer for three years in return for the service. It is of particular interest to note that after the first three years many of these farmers are requesting an up-date of the plan in return for another fertilizer contract.

I.C.I. CASHPLAN converts farm plans into money. It converts cropping and livestock plans from physical numbers and acres into financial terms and gives a complete picture of the financial consequences of alternative management decisions.

It shows the effect of changes in the plan on monthly cashflow; on annual profit; and on the capital build-up within the farm business.

Again, this relatively new service has been welcomed by both farmers and financial advisers, particularly bank managers, so we would expect some 500 farmers to participate in the service in 1974.



The major feedingstuff and fertilizer manufacturers in the U.K. have always provided a free technical service to their farmer customers. There is now a growing tendency to provide this service whether technical or management orientated in return for business not tied to price. The growth of this type of contracting in the future will depend upon the availability of similar services from government agencies and the level of fees being charged by private consultants.

The U.K. is well ahead of its partners in the E.E.C. in the provision of practical farm business aids to farmers by suppliers. As farms in other E.E.C. countries tend to be smaller than in the U.K. contracting on the lines discussed in this paper would seem most likely to develop alongside the various farmers cooperatives which are so important in most European countries.



