

FACING THE FUTURE

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ORIGINS OF THE PROJECT

Progressive Pork Producers Co-Operative (3P) was formed for the sole purpose of vertically integrating the hog farming members to the next stages of the pork supply chain. Those stages are hog slaughter and fresh pork preparation. The seeds of the concept were planted at an Ontario Pork annual meeting in the mid 1980's, with a discussion about a producer-operated kill and chill plant. Subsequently, Ontario Pork commissioned a study of the possibilities and concluded that the project was not feasible under that banner. However the concept did not die and in 1993 Progressive Pork Producers Co-Operative Inc. was formed with the intent of finding a suitable entry venue into the hog slaughter and processing business.

Many people found the concept of an integrated system alluring and initially the Co-op had about 500 members. Those 500 members produced about 1,000,000 hogs annually. When members were asked to commit funds to take the idea forward, some dropped out. Many, however, agreed to commit money through a check-off to fund the development of the plan.

With funds from a member check-off, 3P began an intensive study of the potential of various types and sizes of plants. The initial study looked at the costs and efficiencies of a 1,000,000 hog per year plant. As the plan evolved, it became clear that members would need to provide the equity component of the financing package. That represented a significant financial commitment by members and again some dropped out. By this time, the members' production was about 600,000 to 700,000 hogs annually. Our analysis still indicated, that was a feasible size.

The culmination of the project came in 2001 when the opportunity to buy Conestoga Meat Packers was presented. That deal was completed last year when Progressive Pork Producers Inc. purchased the shares of Conestoga Meat Packers Inc. Progressive Pork Producers is now structured as a new generation co-operative.

The plan now is to kill all of the hogs produced by the 173 members and market the meat as fresh pork.

WHY WOULD PORK PRODUCERS DO THIS?

Meat packing is a volatile, high-risk business but it is offsetting vs. the risk of hog farming. The question of why hog farmers would want to take the risk of vertically integrating into meat packing is complex and multi-dimensional. However, the primary reason centers on the question of whether our future as smaller, independent farmers is more predictable with or

without the integration. In order to assess that, we looked at the state of the pork industry in North America. Our conclusions were:

- Demand for the product is declining.
- Supply chain relationships, across segments, are poor.
- Supply chain segments are internally fragmented.
- Vertical markets have failed.
- Most of the North American industry is vertically integrated or aligned.
- The most profitable business in the industry is the most integrated.

Factors Contributing to Vertical Integration

- Vertical market failure – the market becomes so risky and unreliable that it is impossible to make coherent business plans and the contracts designed to overcome that risk become difficult to create and administer.
- Unequal distribution of market power.
- Integration can raise barriers to entry and allow price discrimination across segments.
- Independents are pulling out of adjacent stages of the supply chain.

Characteristics of a Failed Market

- A small number of buyers and sellers.
- High asset specificity, durability and intensity.
- Frequent transactions.

CHALLENGES FOR THE FUTURE

- Operate a new generation co-operative efficiently and effectively.
- Show farmers how their pigs affect the marketability of the product.
- Sell the product profitably.

OBJECTIVES

Through the last ten years, the gross returns per hog have ranged from \$235 to \$30. That volatility is unacceptable for any logical business planner. This project set out to address ways of managing and mitigating that risk. The lives of our members are based on their businesses. Their families' future hangs on successful and stable production. The final membership of the Co-op is comprised of these people....firmly committed members who were willing to risk their capital and agree to provide a consistent supply of high quality hogs. From the beginning of this project, members have been told that their payments would be based on the market value of their pigs. The intent, therefore, is to pursue markets for high quality hogs where the production and control system can be a part of the process. Farmers have traditionally bought branded products (seed grains, herbicides, machinery, feed) and

combined them to produce a commodity. That commodity is then sold to a buyer who takes it apart and produces branded products. 3P believes that how the pigs are grown can be part of the brand.

Pork is the most widely consumed meat in the world. In spite of declining demand, we believe that there is an ongoing market for pork. 3P members intend to face the future by sharing production and processing information, mitigating risk by participating in both sides of the business and by being driven by the customer demand for fresh pork products from integrated, family-based businesses.