

Operating Mechanics of New Zealand's Four Main Rural Retail Businesses

Kelloggs Rural Leadership 2013

Wayne Langford
198 Long Plain Road
Takaka
PH: 03 5257377

Email: goaheadfarms@yahoo.co.nz

Contents

Executive Summary	3
Introduction	4
Objective	4
Limitations	5
Research and Literature Review	5
Summary of Interview with Jono Pavey (ATS)	6
SWOT Analysis ATS	8
Summary of Interview with Jason Minkhorst (RD1)	11
SWOT Analysis RD1	13
Summary of Interview with Stephen Guerin (PGW)	16
SWOT Analysis PGW	19
Summary of Interview with Brent Esler (Farmlands)	22
SWOT Analysis Farmlands	24
Conclusion	26
Appendices	27
Acknowledgements	28

Executive Summary

New Zealand has four prominent rural retailers, Ashburton Trading Society (ATS), Farmlands, RD1 and PGG Wrightson (PGW). Each of these businesses core, is providing farmers with goods and services. Over recent years we have seen numerous mergers and amalgamations, leading to the marketplace we have today.

Each business is having success in different areas, contributing to their ability to provide goods and services on farm at a sharp price. There seems to be little attraction for each business to compete head to head with each other, instead providing a healthy market place of “Low margins, low overhead costs, and input costs.” (Jason Minkhorst RD1)

The future looks bright for each of these businesses, with numerous opportunities and growth strategies available to them all. Of course, this does not come without threats and game changing market place revolutions. The will see constant battling and drive a to see who can claim that number one spot.

Project Objectives

- To create an understanding of the rural retailers in the current environment.
- To establish how each business is competing in today’s fiercely competitive marketplace.
- To highlight areas of possible strengths and weaknesses.
- To give opinion on possible steps to ensure each businesses survival into the future.

Introduction

Three years ago I was fortunate enough to have been elected onto the Executive of the Rural Service Centre (RSC) in Takaka. The RSC has a veterinarian clinic with four vets and a rural supplies store similar to the size of your average rural retail stores throughout the country.

Ever since being involved with the RSC, I have been fortunate enough to see how the business is run from either side of the counter. I have become more aware of trading techniques, marketing and business practices. It is something that I find fascinating.

Over the past ten years, we have seen a massive change in our rural retailers, with smaller merchants being brought out, and large mega mergers, such as PGG Wrightson and CRT-Farmlands. I felt like this was an ideal time now to have a look at where each of these businesses is sitting.

This project was specifically a research project, and not an analysis, pitting one business against the other. Of course there are comparisons to be made, but this is only done to give a clear understanding of the positioning of each business.

Objectives

To understand how our larger rural retailers are combating the fiercely competitive marketplace, and what steps they are putting in place to ensure their survival into the future.

In preparing for this report, I realised that I could not focus on the history of these companies, as it would soon become too large. Instead I focused on the status quo of each business, and possible future outcomes.

Limitations

There is no current literature on this topic, as a review has not been undertaken of these companies on the scale and as in depth as I wanted to examine them in their current environment.

To complete my project I required access to very sensitive strategy and performance information. The parties involved had to also be made aware and understand that the information they were sharing would be made public.

In order to get this information the qualitative interviews had to be carried out with CEO's of very large and busy businesses. Gaining access to these men in a face to face forum was no small feat. They also had to make themselves available for follow-up conversations and final draft read through. All in all it required at least 4-5 hours of these Men's valuable time, something I am very grateful for.

Research and Literature Review

At the beginning of this project I did undertake some research of literature but soon realized that the history of these companies was so rich and diverse that this would be the consumption of an entire project on its own. I decided then to investigate the current environment these major players were involved in and the options for future proofing their business going forward. As I mentioned above there was no current research literature to reflect these objectives especially with the recent mergers which are a real game changer to the rural retail market.

Summary of Interview with Jono Pavey (GM Operations) – Ashburton Trading Society.

Stores - 3
Staff - 80
Locations - Ashburton, Methven, Rakaia (ATS own all their buildings)
Members - 2500
Turnover - \$230m

ATS is a Co-Operative –Farmer owned for 50 years. Its first twelve years of business derived from the board of directors obtaining bulk buying discounts, similar to the ATS card today. The co-operative structure is a benefit to ATS, as it allows all profits to stay in Mid-Canterbury, it allows members to know each of the six farmer board members and it does not require the business to financially report to shareholders. However, the disadvantage is their ability to produce working capital for expansion is more difficult.

ATS is run by its CEO, Neil Shaw. It has a board of directors, consisting of six farmer elected directors and one independent, its chairman is Phillip McKendry. It is important for ATS to be the cheapest price for farmers’ every day. With this in mind, rebates are typically low (<1%), so that farmers are being rewarded for what they purchase at the time of purchase.

ATS has a mentality to create a competitive marketplace. Their predominant markets are dairy and arable farming, where they feel they sit second in the marketplace behind RD1, and PGG respectively. The business has a turnover of \$230m, as listed below;

ATS Card	- \$100m	
Electricity	- \$45m	Note- ATS does not sell PKE feed.
Retail	- \$30m	30% of Retail Turnover is in Agchem
Fuel	- \$25m	
Fertiliser	- \$20m	
Seed	- \$ 7m	

The farmer owned co-operative has been able to invest over the last 50 years. They now own the three buildings for their three stores. As well as this, they have invested in a number of subsidiary companies:

- 100% -Pro-active – Generic Agrichemicals
- 50% share ATS Fuel – Brought to service members when Hinds fuel stop was to close.
- 49% share Coulter Seeds – Seed Dressing/ Treatment plant.
- 40% share Water Metrics – Soil moisture monitoring and measuring.
- 50% share RuralCo Card – A recent collaboration with Ravensdown as a joint venture.

With ATS’s strong influence in the arable sector, they have been able to develop vertical integration within their business. This is through their own generic based agrichemical label, and

also the treating of seed through treatment plant, after buying bulk from farmers.

There is a number of aspects that are critical to their business mix. Firstly is their 2500 members, also the ATS card suppliers, who inter-relate with members to provide over 45% of gross turnover. Also critical to the business mix is the 80 staff,

ATS feels that they have had success with their Retail sales growth. This has been achieved with the opening of two new stores (Methven and Rakaia). Also keeping high stock levels has been a real focus for the business. Customers/Members, expect exceptional customer service, and for goods to be on hand when needed. Ashburton boasts approximately 35 salesmen that can sell a 200litre drum of glyphosate, so if ATS can't have it on farm by the end of the day, then someone else can. This has led to an increased cost of doing business, with the area being over serviced. There were no real recent failures seen in the business, however the emphasis was on growing the business to ensure buying power through market saturation. Without the spread into these new areas, market share could have been lost.

ATS has recently unveiled its next step forward, with a joint venture with Ravensdown Fertiliser Co-op, to provide the "RuralCo" Card. This has been a project to allow growth, and to fulfill a strategy to take ATS forward over the next 5-10 year. This is a slightly different approach, compared with opening up new stores, which begin with high capital costs. ATS were able to bring their card services, while Ravensdown were able to offer their database of clients.

ATS have four technical farm reps, who offer technical advice for farmers, and freight service is used to keep cost of on farm deliveries down. ATS do have a website; however there is no web based business transacted. The comment was made, that farmers are quite happy to buy a plough they haven't seen over the internet from Europe, however they are unwilling to buy a stock-standard drum of Roundup off the ATS website.

ATS has long been a farmer owned business. A unique aspect of the business is the non-farming related items at the front of the store. The rural retail area also sells a number of items which would typically be sold in urban based stores. ATS is a rural retailer that has crossed the Rural/Urban divide, offering home ware and giftware mainly for its existing client base, which is something different to each of its competitors.

SWOT Analysis of ATS:

The below analysis is opinions derived by myself.

Strengths:

- **Location** -Smaller area, easier to service
- **Loyalty** -ATS has a very loyal following in Mid-Canterbury
- **Ownership Structure** -Co-operative, allowing profits to stay in Canterbury
- **Price competitiveness** -Even with smaller scale, ATS is able to compete on price, therefore keeping members loyal to their business.
- **Member Spend** -The average member spend is very high within the business, allowing the business to focus on servicing fewer clients

Weaknesses:

- **Size/Scale** -This affects buying power and overhead efficiencies.
- **Ownership Structure** -The ability for growth is hampered by the Co-ops ability to raise capital.
- **Knowledge of ATS** -With recent arrivals of farmers during the dairy boom, ATS has found it to be a weakness, with most new arrivals not understanding the co-ops ethos, or simply who they are.

Opportunities:

- **Nutrition**
As land prices increase, we will see more intensification of land use in this country. I believe we have seen phase one (irrigation), and the beginning of phase two (increased supplement use) in this area. ATS are obviously aware of this, with investments in irrigation and electricity. I feel there are real benefits for the company focusing on supplementary feeding, and also phase three (specialised feeds). An investment in human capital should be the only capital required, with a number of small feed mills in Canterbury. I think as farmers reach maximum grass production under irrigation, they will look for feed crops such as fodder/sugar beet. I believe the demand for this will come

like the wave of irrigation over the Canterbury plains, and ATS must be ready to capitalise.

- **Animal Health**

With a significant part of the rural market now in dairy, and a large part of dairy spend in animal health; I feel this is an opportunity for ATS in particular to lead the way. Prescription animal remedies (PARs), are a high margin product throughout the veterinarian industry. This is an area of farming business that is relatively untouched by rural retailers, however I feel this is about to change. ATS, with its small number of stores, has the ability to open up this market. ATS, could provide a service, particularly around dry off time, contracting vets to manage large numbers of cows over a short space in time. ATS does not need to put a vet in every store, they can focus on high volume, high margin areas. I understand the agreements in place between ATS and local vet practices, but I question the future of these agreements, should other rural retailers become involved in this space.

- **RuralCo Card**

With the RuralCo card going South Island wide and possibly nationwide, it has the potential to build on the foundation of the ATS card. I think this offers numerous opportunities once it is bedded in, such as the online market place, continual membership profiling and significantly greater scale.

- **New Stores**

The opportunity for new stores is obviously an option. The benefit for ATS is that they have now had their two newer stores open for a number of years, and they can now assess how these are performing. A real bonus is that they will be able to stay in the Canterbury area, and if ATS can achieve greater market share, it opens the door for better agreements with suppliers.

Threats:

- **RD1 Growth**

With RD1 growing its footprint of stores, particularly into ATS's areas, it is critical that ATS keeps its market share in dairy in these areas. The co-op must have a strategy of dairy growth, and compete fiercely to keep the new stores out of town.

- **RD1 – Fonterra Alliance**

We have seen this year, RD1 use Fonterra capital to provide benefits to farmers, with drought relief (3500 farmers) and riparian plantings. RD1 are using Fonterra's database of shareholders to become a large buying group, a very real threat for ATS.

- **Farmlands Scale**

I feel we are yet to see the true benefits of the recent merger to create Farmlands. They will now be directly competing in areas such as card services, fertiliser and agrichemical on a national level. Fostering of relationships with ATS, and clearly defining why a farmer should support the ATS co-operative is essential for ATS. I feel the main area ATS will notice Farmlands presence will be in their retail pricing and also the arable sector, where they try and gain traction in their nutrition business.

- **Availability of human capital**

As any small business will know, the importance of great people is critical. With ATS's smaller scale, the performance of its people must be second to none. Getting great performance from ATS's team needs to be given more attention than any other area of the business. Each of the four businesses I spoke with all mentioned the struggle they had to find quality people, particularly TFR's.

- **Success of Ruralco Card**

The ATS card has become a great success for its Co-op. With the launch of the RuralCo Card, I question whether this success can be continued. I understand the concept of the card, and how ATS wishes to achieve desired results; however I question its ability to achieve this. I feel ATS must offer a reward program with their card. I do not feel they will be able to receive enough rebate difference between stores, over its competitors, so they need to offer something else for customers to use their card. Farmlands card has been very successful, and should only get better with greater scale. Attacking this card in the South Island is quite a risk, and will have to be managed extremely well. Also keeping in mind investment in retail cards may be a short term return, if significant undercutting between competitors occurs.

- **Corporate Farming**

Corporate Farming is increasing in NZ and particularly Canterbury. Understanding the mentalities of these businesses is critical to ATS's success. They should be seen as an opportunity, more than a threat. However, if ATS does not have strategies in place to create relationships with these farms, it will fail. It is very important for the Board to give clear direction on the co-ops ethos around this area. This is something to monitor and change continuously.

Summary of Interview with Jason Minkhorst (CEO) – RD1

Stores	– 69	-9 New Stores on their way
Staff	- 761	
Locations	- New Zealand Wide	
Members	- No Membership	-95% Fonterra Farmers have an account
Turnover	- \$900m	

RD1 is a Co-operative, 100% owned by Fonterra and its shareholders. The business works very hard on creating a “Fonterra environment” for its customers. “A successful RD1 can be the front door to Co-Operative” was how Greg Muir (previous CEO Warehouse and chair of Pumpkin Patch) described the business. RD1 thinks that farmer/owner involvement is “fantastic” and a definite advantage of being a co-op. With Fonterra as a owner, the business does not struggle as much with capital issues as other co-ops, a definite advantage.

RD1 is run by its managing director, Jason Minkhorst. Jason is also on the Board of Directors with two others, who must report back to Theo Spierings, and the Fonterra Board. RD1 returns its profits through the Fonterra dividend, making up \$.02c of the dividend last year. RD1 is actively developing a loyalty scheme whereby profits are returned to members that actively support RD1.

RD1’s focus is on the dairy sector and getting the dairy sector right. They pride themselves on running a slick and efficient business, dealing with low margins, low overheads and low input costs. RD1 had a gross turnover of around \$900m last year. It’s earnings before interest and tax was \$32m. Gross turnover was made up by the following,

- Retail -\$500m -Including fuel, card and fertilizer.
- Feed -\$400m

RD1 does not have as many subsidiary investments as the other rural retailers. However it does have significant investment in two of its main profit streams;

- 50% INL - Importing PKE and Molasses
- NZ AgBiz - Manufacturing of milk based feed products.

Vertical integration is not a major part of RD1’s business model. The products they create with their NZ AgBiz business, such as calf milk powders and other nutritional products, allows RD1 access into young stock programs with their customers. The shareholding in INL, allows for importation of feed, especially in the North Island, with RD1 selling 450,000tonnes of PKE, and 140,000tonnes of Molasses.

Critical to RD1’s business unit mix is “Getting Dairy Right”. RD1 prides itself on being the largest purchaser from NZ dairies top 20 suppliers. By maintaining market share, RD1 will be

able to access product at competitive prices, and try to dominate the dairy market.

RD1's success has been highlighted in this recent dairy season. With drought crippling much of the country, RD1's ability to offer 'Drought Packages' of six months interest free to 3,500 Fonterra farmers, was a way for the business to give back to their customers in their time of need. Also with the involvement with Fonterra, RD1 has been able to offer fantastic deals for fencing waterways and other environmental compliance issues coming this season. While there has been success, failure to capture the lifestyle market, through the more lifestyle based stores has been seen as a slight chink in the armour.

As mentioned above, RD1 is still looking to increase its footprint of stores. Its focus is having stores in areas where milksolids are. Leeston, Culverden and Murchison are examples of new stores coming, as well as others further south. RD1 lease's all of its stores which frees up capital for other areas of its business. Capital will need to be spent keeping the business modern and evolving with the dairy industry. The development of their online catalogue will look to increase online business, which is already gaining traction with PKE and calf milk powder.

RD1, have over forty technical sales reps (TSR's). Recent advertising has promoted their ability to bring goods to the farmer. This is a concept that has moved from being a service, to being a standard that is expected from farmers, therefore increasing the cost of trade.

As mentioned above, RD1 has had a dabble at the rural/urban divide, by opening lifestyle based stores in such areas as Taupo, Rotorua, Hamilton and Whangarei. With the high cost and slow turnover of stock, as well as the increased staffing required, it is seen as an area that they may choose to back away from. RD1 also offers a card service with over 2000 retail outlets, they have recently brought card services in house to cut cost. The RD1 card does not offer rewards points.

SWOT Analysis of RD1:

The below analysis is opinions derived by myself.

Strengths:

- **Owned By Fonterra** -95% Fonterra Farmers have an account
- **Scale in Dairy** -Buying power, top purchaser of top 20 dairy supplies
- **Ownership Structure** -Allows access to capital, greater than other co-operatives
- **Rebate returned to Farmer** -Profits are returned to farmers through Fonterra milk payment
- **No debtors** -Due to deduction made from Fonterra milk payment
- **Price** -RD1 can offer to farmers that it won't be beaten on price

Weaknesses:

- **Locations** -Currently the business is in the process of opening stores, increasing its footprint, particularly in the South Island
- **Fonterra Owned** -Unfortunately, one of RD1's strengths, is also a weakness. With Fonterra not being popular amongst some farmers, it can make it difficult to trade. Also the opportunity to open stores down the West Coast of the South Island is difficult, with no Fonterra suppliers. Note; Synlait is a large RD1 customer.

Opportunities:

- **Nutrition**
As land prices increase, we will see more intensification of land use in this country. I believe we have seen phase one (irrigation), and the beginning of phase two (increased supplement use) in this area. RD1 are obviously aware of this, with an investment in INL. I feel there are real benefits for the company focusing on supplementary feeding, and also phase three (specialised feeds). This will not only need investment in product, especially importation, but also in human resources, an area RD1 must gain ground in.

- **Animal Health**
 With a significant part of the rural market now in dairy, and a large part of dairy spend in animal health, I feel this is an opportunity for a rural retail trader to delve into the prescription animal remedy (PAR) market. However, I do question if this is right for RD1. Firstly it will cause dis loyalty amongst its shareholder members, it will also open Fonterra up to be attacked about the miss-use of animal pharmaceuticals, and I don't think RD1 would be able to achieve appropriate veterinarian staffing to achieve this result.
- **Online Market Place**
 With the advancement of technology and an increased cost of servicing farmers, it is critical for RD1 to create an online marketplace. Also, the opportunity still exists to be the "first". PGW have begun this process, with Agonline, now adding some product mix, as well as livestock. RD1, are also just entering this space. This will be critical I feel when the new loyalty scheme is released, allowing Fonterra farmers without an RD1 store to purchase goods.
- **Card** -
 The card has become a critical success for two of RD1's competitors. If RD1 are to compete in this area, I feel they must offer a reward program with their card. I do not feel they will be able to receive enough rebate difference between stores, than its competitors, so they need to offer something else for customers to use their card. Note, that the Farmlands card is very successful, and investment in retail cards may be a short term return, if significant undercutting between competitors occurs.
- **Dividend Structure**
 A new loyalty scheme returning RD1 profits back to its members who use the business, instead of the entire Fonterra shareholding, will have a dramatic effect on RD1's competitiveness. The return will be a figure that farmers will not be able to ignore. RD1, will need to be careful however. It will need to be able to offer the same goods and services to all of its members for this type of structure to be fair, otherwise it could create great disharmony amongst shareholders.
- **Opportunity for new stores -**
 RD1 is yet to create a footprint over the entire country! With every one of its stores making money, it really would be unwise to stop until the business has complete saturation of Fonterra farmers.
- **Merger**
 RD1 is New Zealand's premium dairy rural retailer. RD1 has 90% of its business in dairy, 75% of PGW's business is non-dairy, so a merger could seem an obvious option. However, I feel RD1 has a real strength in being the best in its field. I do not see Fonterra

wanting to make an investment in PGW, and I think RD1 will lose a lot of its competitive advantages if it is not owned by Fonterra.

Threats:

- **PGW's Dairy Strategy**

PGW has openly stated that it wants to increase its market share in dairy. PGW is a business that runs a different model to RD1, one which could entice farmers over. RD1, must be strong on price, and the best on service.

- **Palm Kernel Extract Marketplace**

Over 40% of RD1's gross turnover is from PKE sales. Although margins are very low on this product, the volume sold makes it a margin worth having. Increased pressure from PKE opponents and possibly Fonterra customers, could put real pressure on RD1's ability to import PKE into the country. Also increased technology at processing could see the feed value of PKE drop to a level which is not attractive to farmers.

- **Farmlands Scale**

I feel we are yet to see the true benefits of the recent merger to create Farmlands. They will now be directly competing in areas such as card services, finance and livestock on a national level. RD1 needs to compete differently with Farmlands. RD1 will need to remain cheapest on price, but also offer significantly better loyalty returns than what Farmlands does through its rebates.

- **Reliance on Dairy**

With dairy making up 90% of RD1's turnover, recent price fluctuations in dairy commodities have put significant pressure on business performance. Obviously with RD1's reliance on dairy, it must manage such fluctuations, and also help farmers manage fluctuations, so that the business doesn't end up significant losses in profit each year.

Summary of interview with Stephen Guerin (GM Retail) - PGG Wrightson

Stores	-99	-Down from 110 at peak
Staff	-580	-Retail Staff
Location	-NZ Wide	-49 North Island 51 South Island
Members	-No Membership	
Turnover	-\$1.13b	-Total group turnover

PGG Wrightson (PGW) is a Christchurch based multinational formed in October 2005 through the merger of Pyne Gould Guinness Ltd and Wrightson Limited, which together combine a rich history of over 150 years – dating from 1851 and 1841 respectively. PGW has customers all over the world, particularly with its seed business, but also rural retail in South America.

Being New Zealand's only public listed rural retailer has both its advantages and disadvantages. PGW now has the ability to raise capital a lot easier than that its competitors. It also has a degree of transparency which elevates it to a position where it must analyse its business more rigorously. PGW governance is different to the other co-ops, without farmer elected directors (Trevor Burt is a board member, also chairman of Ngai Tahu Holdings, and has personal farming interests in the South Island). Its directors are experienced in running a business from above, with little involvement at the shop floor. One of the disadvantages with the publically listed company is that all their performance statistics and profit margins are published for not only the public to analyse but also PGW's suppliers and competitors. This is a unique advantage to its competitors. Another disadvantage that can occur is when the company has block ownership of its shares, currently with a Chinese investment, but previously with the Rural Portfolio Investments (owned by the Norgate and McConnon families) and also Fletcher Challenge. This draws attention away from who PGW is, and onto whom the investor is, sometimes clouding people's perception of the business.

PGW's core in retail is based around the quality of its people. They believe they have the best technical experts on farm, providing not only excellent advice but also quality products to back them up.

PGW has a new CEO, with Mark Dewdney taking over in July this year. The company has a board of seven directors, with Guanglin Lai (Alan) becoming the new chair after the recent AGM. The business has just over 754 million shares, valued at \$.43cents, 05/11/13.

PGW's historic focus has been with the sheep and beef industry. PGW has also invested heavily in seed, and now world class the seed division as the backbone of their business. Its business is broken into six main areas, with a total turnover of \$1.13bn;

1.	Retail	-\$433m	-Includes Fert Rebate only
2.	Livestock	-\$98.5m	
3.	Wool	-\$79.5m	
4.	Real Estate	-\$24.2m	
5.	Insurance & Finance	-\$3.7m	
6.	Irrigation & Pumping	-\$45.1m	
7.	Ag NZ	-\$4m	
8.	Ag South America	-\$21m	
9.	Seeds & Grain	-\$308m	
10.	Agrifeeds	-\$13.6m	
11.	South America	-\$98m	

PGW has its core sectors listed above. It's ability to share premises and combine corporate resources such as HR, IT, and Finance have helped streamline the business. It does have a large number of subsidiaries, which are tied into the categories above. One subsidiary of note is;

- 50% Share in Agrifeeds (the other 50% owned by INL)

Vertical integration has been the core of PGW. With such a successful grain and seed division, TFR's are able to push products on farm. Even with the increase in dairy conversions on the Canterbury Plains, PGW are still finding cropping volumes going up. This is due to the increase in irrigated land and increasing yields. PGW is also finding that dairy support is growing their business with more fodder and maize crops. Whether it be the land you buy to plant your crop on, your seed, your water or your sale point, PGW has the opportunity to be involved.

Critical to the success of PGW is its people. Eighty five per cent of sales are completed by a Technical Farm Rep. This is why it is critical that PGW invest in the intellectual property of its people, such as training older staff on modern technology. An interesting time is coming for PGW, with 50% of new TFR applicants being female. This will add a different dynamic not only to their staffing profile, but also to customer relations. An important area is the relationship with supply partners, ensuring product arrives at the right time and the right price to remain competitive. Seed is a critical corridor, as it opens the door for the agrichemical and fertiliser market, which have a significant impact on PGW's bottom line.

PGW has had recent success in growing market share, particularly with agchem, fertiliser and seed. Also the business has been able to lower its debt from \$400m to \$100m over the last five years. However it does have it challenges, adapting to the increasing dairy boom, and recently with Merial making drench vet only product.

Into the future PGW is already making significant investment into the irrigation market, which as mentioned above, vertically flows through their business. Animal nutrition was also highlighted as a possible opportunity for growth as New Zealand not only has more dairy cows, but is beginning to learn the importance of balanced feeding.

PGW were the catalysts for the TFR's on the road. Due to the businesses strong sheep and beef background, it made sense to take the business to the customer. This has only continued, focusing on advice rather than delivery. Modern technology such as email, cell phones and text messages are becoming a tool to connect with customers, but the TFR is still seen as the essential sales tool.

PGW have stayed out of the urban market, insisting that rural merchants need to provide a quality product and service. PGW offers a PGW visa card, which is their first step in ramping up competition in the card market where others have had success.

SWOT Analysis of PGW

The below analysis is opinions derived by myself.

Strengths:

- **Location** -NZ wide
- **Well Established/History** -Every farmer knows PGW
- **Scale** -Buying power, providing service and expertise
- **Multinational** -Growing business internationally
- **Vertical Integrations** -Seed to Feed
- **Ownership Structure** -Allows access to capital
- **Retail Business Model** -Different to that of other competitors with strong focus on technical farm reps.
- **Access to Saleyards** -PGW Monopoly
- **R&D Capabilities** -Potential to retail seed before it is made available

Weaknesses:

- **Ownership Structure** -Limited control on who owns shares, which can affect customers perceptions of the business
- **Companies History** -The company has such a rich history, that it now becomes difficult to change customers perceptions, for example, PGW being a Sheep and Beef store when it is now trying to move into the Dairy market.

Opportunities:

- **Nutrition**
As land prices increase, we will see more intensification of land use in this country. I believe we have seen phase one (irrigation), and the beginning of phase two (increased supplement use) in this area. PGW are obviously aware of this, recently investing in irrigation. I feel there are real benefits for the company focusing on supplementary feeding, and also phase three (specialised feeds). This will not only need investment in product, but also in human resources, an area PGW prides itself on.

- **Animal Health**
 With a significant part of the rural market now in dairy, and a large part of dairy spend in animal health, I feel this is an opportunity for PGW in particular to lead the way. Prescription animal remedies (PARs), are a high margin product throughout the veterinarian industry. This is an area of farming business that is relatively untouched by rural retailers, however I feel this is about to change. PGW are not a co-operative, and can offer services in parts of the country and not others. They do not need to put a vet in every store, they can focus on high volume, high margin areas.
- **Online Market Place**
 With the advancement of technology and an increased cost of servicing farmers, it is critical for PGW to create an online marketplace. Also, the opportunity still exists to be the “first”. PGW have begun this process, with Agonline, now adding some product mix, as well as livestock. The ironic aspect of an online market for PGW, could be similar to their earlier days, where agents were used to take product to farmers, hence creating technical farm reps, and the business model they use today.
- **Card**
 The card has become a critical success for two of PGW’s competitors. If PGW are to compete in this area, I feel they must offer a reward program with their card. I do not feel they will be able to receive enough rebate difference between stores, than its competitors, so they need to offer something else for customers to use their card. Note, that the Farmlands card is very successful, and investment in retail cards may be a short term return, if significant undercutting between competitors occurs.
- **International Business**
 This is an area I do not have a lot of experience in, however I am aware that growth in South America and other countries will lead to more scale and buying power. This will increase your competitive advantage with competition in New Zealand.
- **Water**
 I feel that PGW cannot underestimate the opportunity of investing into the harvesting, application and measurement of water through irrigation in NZ. A seed needs water to grow, PGW has seeds, so just add water. This will allow for several vertical integrations within the business, and access to customers from a different angle.
- **Merger-** RD1 is New Zealand’s premium dairy rural retailer. PGW must consider options of wether to try and gain market share, or purchase market share. My own opinion is that PGW should compete, using their business model with TFR’s on the road. If this model was successful whilst dealing with Sheep and Beef customers, then there is no doubt it can be a success with Dairy clients who’s spend is on a low number of items, in a large volume. The key is scale and buying power, which PGW has.

Threats:

- **RD1 Growth**
With RD1 growing its footprint of stores, particularly into PGW's areas, it is critical that PGW keeps its market share in dairy in these areas. The company cannot have a strategy of dairy growth, but then roll over easily when a new store comes to town.
- **RD1 – Fonterra Alliance**
We have seen this year, RD1 use Fonterra capital to provide benefits to farmers, with drought relief (3500 farmers) and riparian plantings. RD1 are using Fonterra's database of shareholders to become a large buying group, a very real threat for PGW.
- **Farmlands Scale**
I feel we are yet to see the true benefits of the recent merger to create Farmlands. They will now be directly competing in areas such as card services, real estate and livestock on a national level. Fostering of relationships with PGW, and avoiding the pull to a farmer owned co-operative is essential for PGW. I feel the main area PGW will notice Farmlands presence will be in there retail pricing.
- **Availability of human capital**
The reason why farmers are asked to shop at PGW, is because of the "quality of their people". Each of the four businesses I spoke with all mentioned the struggle they had to find quality staff, particularly TFR's. From what I have seen, PGW are putting incredible effort into training, motivating, managing and retaining staff. PGW need to be leaders in this area and be employers of choice. I think it is important to start developing systems that removes human capital from one area, so that it can be used in areas of more significance, ie AgOnline.

Summary of Interview with Brent Esler (CEO)-Farmlands

Stores	-80	-18 Real Estate offices
Staff	-1170	
Location	-NZ Wide	-48 North Island 32 South Island
Members	-56,000	
Turnover	-\$2.2bn	

Farmlands is our largest rural retail co-operative. A merger on 1st March 2013, brought Farmlands from the north, together with CRT from the south. Both companies with a rich fifty year history in rural retail now have a combined membership of 56,000 and total turnover of \$2.2billion.

Farmlands feel there are some real advantages to being a co-operative. The objectives of the customer and the shareholders are aligned which helps provide far better service to its members. With the average shareholding at \$2000, customers aren't members of Farmlands looking for a dividend on investment. Also staff is dealing with people that own the business so therefore should be looking for the same result. The other strength is that suppliers will now not give a natural advantage to one company over another, therefore buying power with size and scale will lead to higher rebates, benefitting the co-op.

The potential disadvantage for a co-op is slow moving decision making. This has been seen in recent years with numerous mergers and acquisitions. With all members being given the opportunity to speak, and farmer parochialism often decisions can become stagnated.

Farmlands is run by CEO, Brent Esler. It has a board of directors consisting of eight farmer elected directors. Lachie Johnstone is the current chairman of the board. The co-op aims to rebate 75% of its operating surplus each year, generally around 50 % in cash and 50% in shares. No one shareholder can have more than \$15,000 in shares under current rules.

Farmlands exists for one simple reason, to use the collective power of the shareholders to negotiate better deals and improve individual profitability across all forms of agriculture. Its \$2.2bn in turnover can be divided into three main areas:

1.	Retail	-\$910m
2.	Card	-\$590m
3.	Fuel & Oil Distribution	-\$630m
4.	Services	-\$ 4m

Farmlands must register their finance and real estate division separate from the co-op, but this is a technicality. The only other subsidiary is Farmlands Fuel, which is the largest independent distributor in NZ and equates to approximately 10% of NZ fuel. Farmlands fuel is 100% owned by Farmlands, and has been distributed under the CRT brand in the North Island for the past five years.

Farmlands has been able to achieve vertical integration in its feed business, taking advantage of being able to sell seed, agchem, fertiliser and fuel. Then being able to buy the crop and either sell it as a commodity to other farmers, or process it into a form that customers can use

it. Farmlands processes 40% of the grain crops it buys in its own mills. This way they are avoiding being price takers, and taking the manufacturing, wholesale and retail margins. Other vertical integrations are its generic items in store, such as “Backroad” clothing, this has been one of the company’s strongest performing items over the last ten years.

Sharp price’s and exceptional service in rural supplies, as well as great card offers are seen as critical in the business mix of the co-operative. They can do all the marketing and promotion they like, but if they don’t get this area right, their business will not be a success.

One of the larger successes that Farmlands has seen over the last ten years has been CRT Fuel. They have been able to become New Zealand’s largest independent fuel distributor with minimal capital investment. The co-operative had investment into the wool industry for ten years until 2003. The idea to sell product after the farm gate was not a good option. Although it didn’t cost the co-op, with a breakeven result over the years it operated, it did prove volatile and became a management distraction.

Farmlands had bold predictions of doubling the operating surplus after the merger. It is felt that the scale of the new co-operative is opening more doors than expected and the business has the potential to “blow merger predictions apart.” As you can imagine, a strong growth curve is predicted.

Farmlands has stayed out of palm kernel importation, due to uncertainty of palm kernel processing into the future. It already has a strong grain based feed division, however it is aware of the potential for this market into the future.

The CRT card has been a true success. It has over 5000 suppliers, it is easily the largest used agricultural card, with over 125,000 cards in circulation. Something that is different about the CRT card, is that it offers a rewards program. So not only has the card become valuable, but the reward program is also starting to provide valuable returns. It is providing farmers with something they simply can’t ignore once they get it.

CRT Farmlands have met the rural/lifestyle divide down the middle. They identify and cater for the lifestyle market, recognizing the 6000 new lifestyle properties coming onto the market this year. The customers have high service costs, but if they can move them through the stores in volume, then they significantly increase throughput of high margin products. The CRT Farmlands card has taken a step into the urban market, taking a percentage return off each purchase, without causing a fight back from its urban counterparts, such as the Warehouse, or Pak n Save.

SWOT Analysis of Farmlands:

The below analysis is opinions derived by myself.

Strengths:

- **Location** -NZ wide
- **Well Established/History** -Every farmer knows Farmlands
- **Scale** -Buying power through recent merger
- **Loyalty** -56,000 members
- **Ownership Structure** -Allows for returns back to farmers
- **Farmlands Fuel** -Nationwide fuel distribution
- **Farmlands Card** -The most successful rural retail card at the moment

Weaknesses:

- **Next Stage of Growth** -Farmlands recognises that all the easy fruit has been picked already, and the next stage of growth will be harder.
- **Scientific Analysis Animal Health** -An area where Farmlands are looking to focus in their business, but are struggling with the human resource in this area.

Opportunities:

- **Nutrition**
As land prices increase, we will see more intensification of land use in this country. I believe we have seen phase one (irrigation), and the beginning of phase two (increased supplement use) in this area. Farmlands are obviously aware of this, with investment into bulk feed handling. I feel there are real benefits for the co-op to focus on supplementary feeding, and also phase three (specialised feeds). This will not only need investment in capital, but also in human resources, two areas I feel Farmlands are leading the way with..
- **Animal Health**
With a significant part of the rural market now in dairy, and a large part of dairy spend in animal health, I feel this is an opportunity in the Prescription animal remedies (PARs) market, they are a high margin product throughout the veterinarian industry. This is an area of farming business that is relatively untouched by rural retailers, however I feel this is about to change.

- **Online Market Place**

With the advancement of technology and an increased cost of servicing farmers, it is critical for a business to create an online marketplace. Also, the opportunity still exists to be the “first”. PGW have begun this process, with Agonline, now adding some product mix, as well as livestock. RD1 are also due to release their version, indicating competition is heating up in this marketplace

- **Dairy Support**

With the dairy boom in full swing, there is an opportunity to create a “Dairy Support Program”, involving farmers wintering cows and rearing young stock. The benefits for this come in the livestock division, but also in retail, with Fodder Beet becoming a major player in the market over the next ten years. Management of crops and cows will be essential, as both are high risk and provide the opportunity for off farm expertise.

Threats:

- **RD1 Growth**

With RD1 growing its footprint of stores, particularly into Farmlands areas, it is critical that Farmlands keeps its market share in dairy in these areas.

- **RD1 – Fonterra Alliance**

We have seen this year, RD1 use Fonterra capital to provide benefits to farmers, with drought relief (3500 farmers) and riparian plantings. RD1 are using Fonterra’s database of shareholders to become a large buying group, a very real threat for Farmlands

- **Threats to Card Services**

With the Farmlands card having a turnover greater than \$500million, it will likely come across opposition from its competitors. The new RuralCo card, by ATS, is directly targeting unhappy Farmlands card suppliers, these are suppliers who are not happy with Farmlands card being available at large chain stores. The threat also comes from competitors undercutting suppliers until there is no value left in providing a card service to farmers.

- **RD1 – PGW Merger**

RD1 is 90% Dairy, PGW is 75% non-dairy, the merger makes sense right? It is not quite that simple, and I doubt it will happen any time soon, but when considering buying power/rebates, Farmlands needs to investigate the result should this happen and change the marketplace.

Conclusion

In conclusion, I would like to emphasise how much I have learnt over this project. I would like to leave you all with a quick snapshot on each business;

1. **RD1**

The dairy retail co-op, a smooth, slick operation. A business firmly focused on profit results each year. RD1 are focussed on doing dairy, and getting it right. They have enormous capital behind them (Fonterra), and once they have finished stamping their footprint across the country, will focus on increased sales, and returning profits to loyal members. Don't forget, they could be feeding half the cows in the country?

2. **Farmlands**

The new mega merger, who are looking to answer their critics and smash pre-merger predictions out of the water. This co-op, wants you to use its retail card in every store you purchase, and will potentially be the rural retailer who kept the urban stores out of the rural market. They now have an interesting time taking southern ideas north, and northern ideas south. The card and fuel is a great success, however their retail arm is continually changing rural retail, pressuring other retailers to perform better. We have seen the birth, now what is this big baby going to grow into?

3. **ATS**

This smaller co-op may be smaller, but it can pack a punch like the big boys. ATS is currently undertaking the start of a new strategy, with a new card. This is something that will add to a business that not only battles with the big boys, but keeps its own in Mid Canterbury. This business must focus on quality of its relationships with its members, both at present and into the future.

4. **PGG Wrightson-** The sleeping giant, someone I think has found the key, and is about to start this machine up. With its numerous vertical integrations, its scale both national and international, and its new firm foundations, PGW is a real threat to the marketplace. Not only will they improve what they are doing, I see PGW as the retailer most likely to change business practices in the retail sector, in the near future.

I think there is still room for three national players in the market. As long as ATS keep its loyal members, they will keep their Mid-Canterbury stronghold. The battle for all the retailers will be keeping their service standards high and prices low enough to compete. Therefore I recommend to the customer, that you value the retailer who is investing in you! If they are not, head down the road, because one of the others will be happy to take their place.

“Researching the operating mechanics of our rural retail trading businesses in NZ”

The idea of this project is to research how our four main rural retail stores (RD1, PGG Wrightsons, CRT-Farmlands, ATS) run their businesses. As I do not have a specific question that I would like answered, I have stated that I’m researching these businesses. However, I have narrowed my study down into three main areas:

(Please note: These are a guide, and not the specific questions.)

Ownership Structure:

- Co-operative or private company?
- What are the advantages and disadvantages of each of these ownership structures?
- How does the ownership structure effect the day/day running of the business?
- In what way does your ownership structure impact on senior management and governance of your business?
- What impacts do your subsidiary companies; have on your rural retail trading businesses?
- What is the asset mix of the company, where are you choosing to spend your capital?

Business Unit Mix:

- A look at how each business derives their profits?
- How do vertical integrations from within the business affect the retail profile?
- What is critical to your businesses mix of product and services?
- In what areas, has your businesses had success, and what has not gone so well?
- Is there any other area in which your business is looking to move in the future?

Size and Scale:

- Stores, Staff, Locations, Customers, Members?
- Current financial analysis and future predictions?
- Is bigger better?
- Potential for expansion or consolidation?
- On farm services, and how you use these to connect with customers/members?
- Bulk sales, trading cards, reward programs and what they offer your business?
- Rural/Urban divide and the benefits of crossing over to the other side?

The reason why I have chosen this subject is because I have a genuine interest in this area. I’m currently on the board of directors of a small rural retail trading store/vet clinic (Rural Service Center), and it intrigues me to see how much larger rural retailers are combating the fiercely competitive marketplace, and what steps they are putting in place to ensure their survival into the future.

Acknowledgments

I would like to thank the following people that have given me their support in numerous ways (time, sponsorship and support)

Jono Pavey (ATS)

Neil Shaw (ATS)

Brent Esler (Farmlands)

Stephen Guerin (PGW)

Mark Dwedney (PGW)

Jason Minkhorst (RD1)

Dave Egan (RSC)

Thank you for all your time you have given me in the face to face interviews and follow-up phone calls. Thank you for all your critique and insight into not only my project but also my governance pathway.

Rural Service Center

CRT – Farmlands

Tru Test Milk Hub

For their generous sponsorship

Thank you to my family and farm staff, who made it possible for trips away and late night project work, allowing for a silky finish.

Thank you to my fellow Kelloggers, the alumni, tutors and organisers for this fantastic opportunity.

Last but not least, my wife, and three boys, the backbone of the man that I am.

Thankyou

WAYNE