

The Role of Group Action in the Post-Modern Food System: Working With Buyers

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Opportunity and investment in the post-modern economy

- Tremendous Global Activity in the Post-Modern Agri-food system
 - Global Threats and Opportunities
 - Global Sourcing
 - Massive Amounts of Investment
 - Fragmentation of Demand
 - Dynamic End-user Needs
 - Service and Knowledge Bundling
 - Multinationalism
 - Firms and regions units of analyses
 - Not nation-state unit of analysis

My Thesis

- US marketing cooperatives have not been significant players
 - Why ?
 - Traditional and New Gens have struggled
 - Group action though thrives, just not as self-organized

- 1. Cooperative redesign (80's and 90's) only half the story
Plus...
- 2. Need an industrial marketing perspective
Equals...
- 3. A new strategic architecture for group action

- Two Topics: Cooperative Theory and Industrial Marketing-- then link the two
 - "becoming buyers' agents not sellers' agents"

Co-op Theory

Modern Theory (1940-1980)

- Co-op comparable and competitive with proprietary firms
 - Emilianov (1942); Phillips (1953); Helmberger and Hoos (1962), Ladd (1974), Zusman (1982)
 - Rationality and Stability
 - Homogeneity and Stationarity
 - Conditionality

Neo-Modernists (1980-2000)

- Broke with modern theory
 - Identified organizational design flaws
 - Heterogeneity
 - Dynamics
 - Rational patrons
- Staatz (1983) Game Theory
 - Subadditivity and Harm
- Sexton (1986) Game Theory
 - Pricing and Participation
- Cook (1994) Neo-Institutional
 - Property rights
- Goldsmith (1995) Neo-Institutional
 - Transaction Theory
 - Existence/Senescence and Governance Choice
 - Co-op as a means not an ends

Neo-Modern “Co-ops”

- Consistent with the Prescription of the Neo-Modernists
- New Generation Co-ops and LLCs
 - Growth in New Gens/LLCs
 - 252 (Merritt et al, 2003)
 - K Sourcing (liquidity)
 - Commitment (obligation)
 - Quality (closure and differential pricing)
 - Governance (hierarchical)
 - Resources (core competencies)

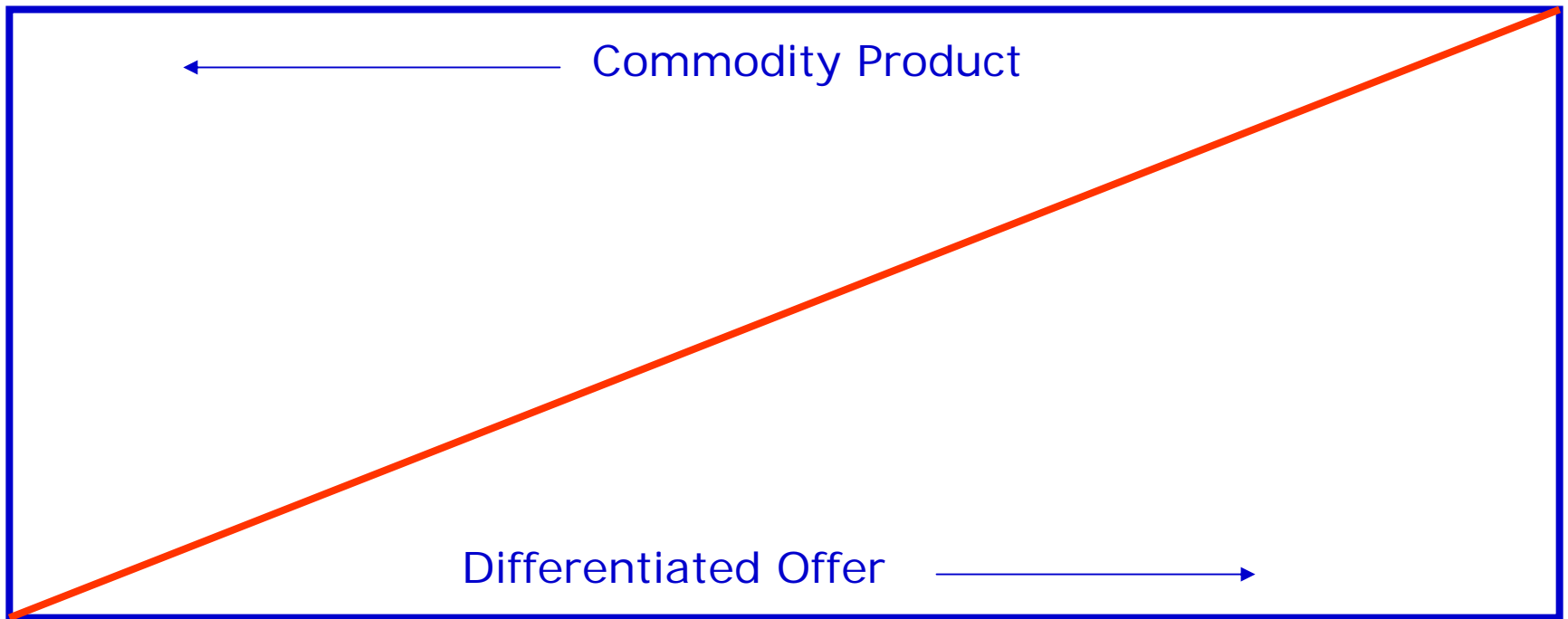
Organizational Implications

□ TC

NGC

LLC

Producer Focus



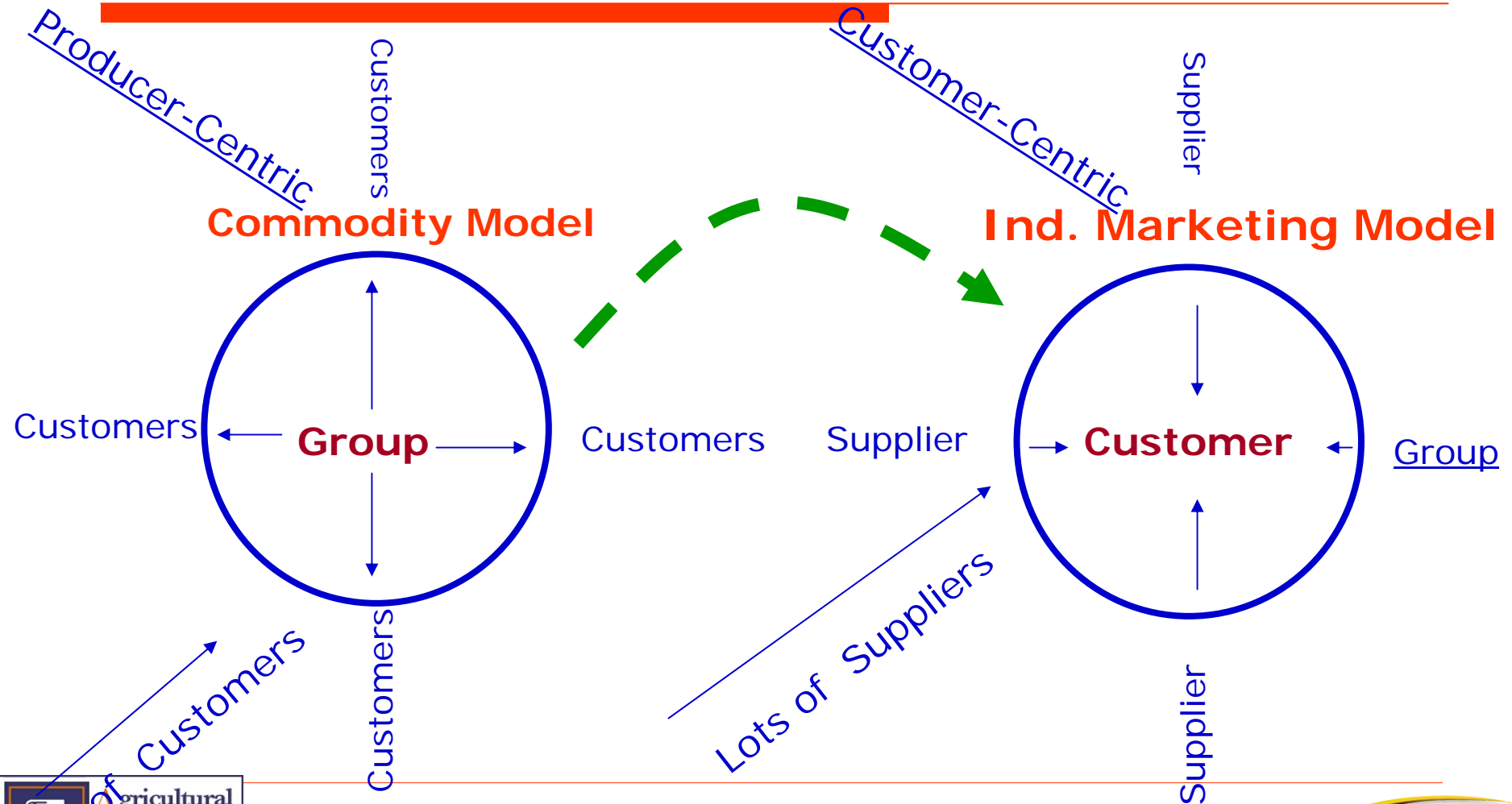
Neo-Modern “Co-ops”

- Organizational Design Changed
 - So what is the problem?
- Modernists and Neo-Modernists
 - Still the same in one key area
 - Still has an “inward” focus
 - We got the org. design correct but missed a critical aspect
 - E.g. Meadowbrook Farms
 - Cooperative existence: Address an internal weaknesses
 - Cooperative existence: Address an external opportunity/need
- Instead offer:
 - Post-Modern Cooperative Theory

A Post-Modern Cooperative Theory

- Integrates Structural Reforms of the Neo-Modernists within an Industrial Marketing Environment
- A new strategic architecture
 - Assumes
 - Monopsony power
 - Counter through differentiation not supply management
 - Elasticity of demand
 - Little market failure
 - Farmer as supplier, not producer
 - Knowing your customer
 - Customer centric, not producer centric
 - Supplier deference (“nesting”)

Industrial Marketing Model:



Industrial Marketing

- End-user orientation
 - “guiding the supplier” Kohli and Jaworski, 1990, JOM.
- The evolution to a service/knowledge sector
 - 1st world enterprises
 - Need to do more
 - Disintermediation
 - Differentiation in some form
- Key Question:
 - Why does the buyer want to buy from a group?...
Your group?

Agricultural Suppliers as Industrial Suppliers

□ The Buy-Side Perspective

- Who are we? Our Post-Modern Identity?

□ Are we (our products/services) strategic?

- Mitigate Risk?
- Provide Market Uplift?

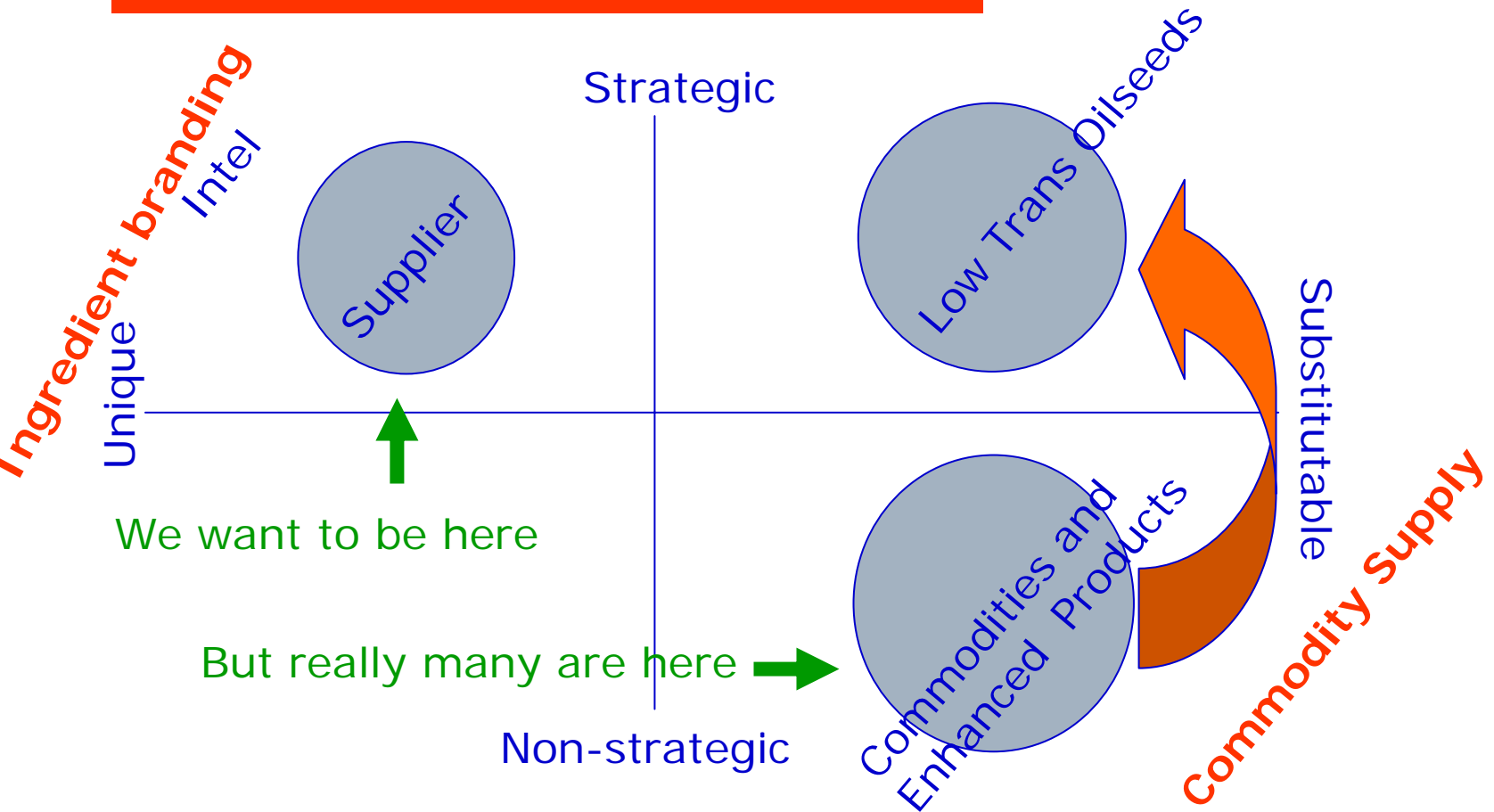
□ Necessary conditions for supra-commodity value creation and capture:

- Buy-Side Strategic Importance
- Inimitability (bundle)

□ **Key reality**

- Asking the buyer to leave the “spot” or
- Asking the buyer to leave current procurement arrangements
- My offer and organization are better

Example: Trans Fats and Supply Chain Management



Differing Perspectives: Case of Trans Fats

----A "Lense" Problem: The Buy Side vs. Sell Side

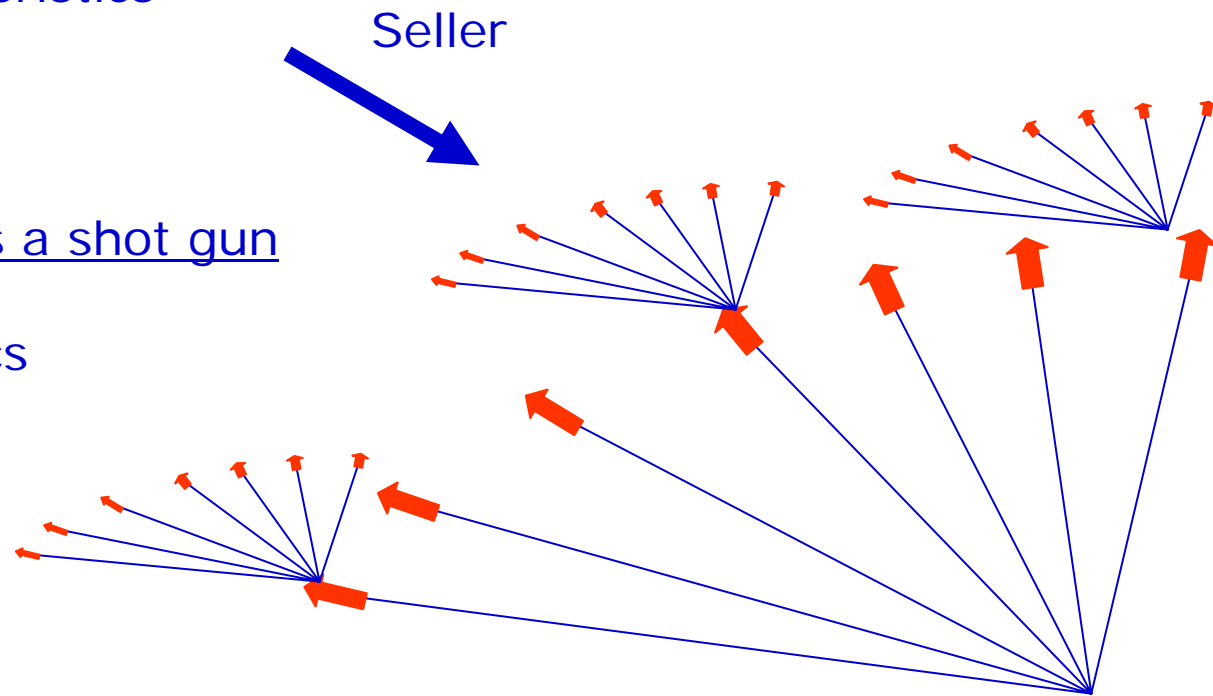
----Looking down the chain vs. looking up the chain

Sell-Side Proposition: Sees a rifle shot

- One Product
- Production Characteristics
- USDA Grade
- Offer Grid

Buy-Side Proposition: Sees a shot gun

- Many Products
- Many Characteristics
- Industrial Needs



Case of Trans Fats: What the Buyer Sees

- Five procurement options available
- 1. Life Science creates a proprietary bean (Monsanto- Vistive® Brand)
- 2. Farmers can deliver low linolenic loads from “commodity” seed (Thumb Oil)
- 3. Processors can deliver low trans fat products from commodity beans (ADM)
- 4. Processors can deliver low trans fat products from commodity oil seeds (Cargill)
- 5. Food manufacturers can adjust formulas and recipes (Strategic)

The bean matters

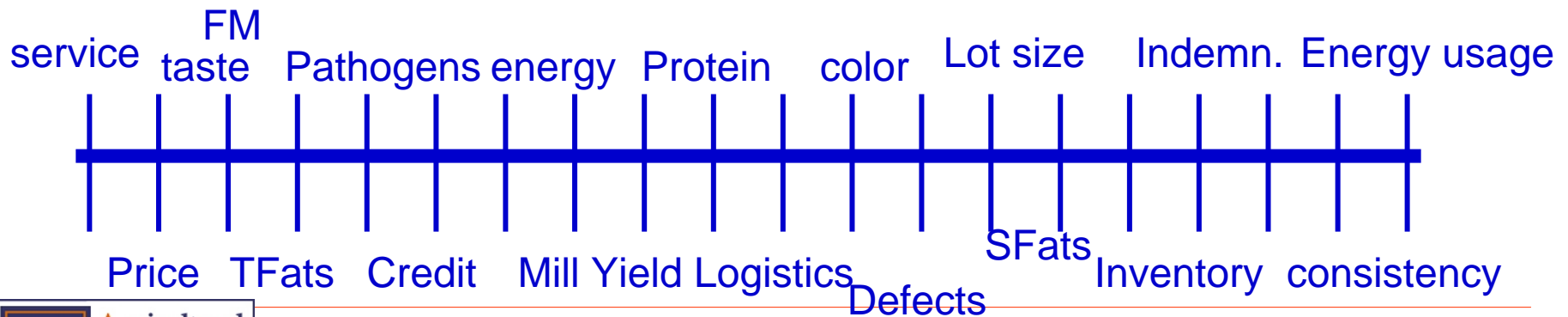
The bean doesn't matter

Case of Trans Fats

- Numerous technological solutions
 - For a buyer what do they mean?
 - Market Discipline
 - Supply Redundancy
 - Risk Reduction
 - Industrial inputs substituting for agricultural inputs
 - Is the “bean” strategic?
 - “enhanced-net weight” meat

For a Buyer: Attributes not Products

- Buyer not necessarily looking for a singular solution
 - Turn to a famous economist, Kelvin Lancaster:
 - Customers buy attributes not products
- First Order Factors: Price, Risk, and Supply Variability (Goldsmith et al, JCNS, 2002 case of meat in Chicago)
- 2nd Order Factors: Quality



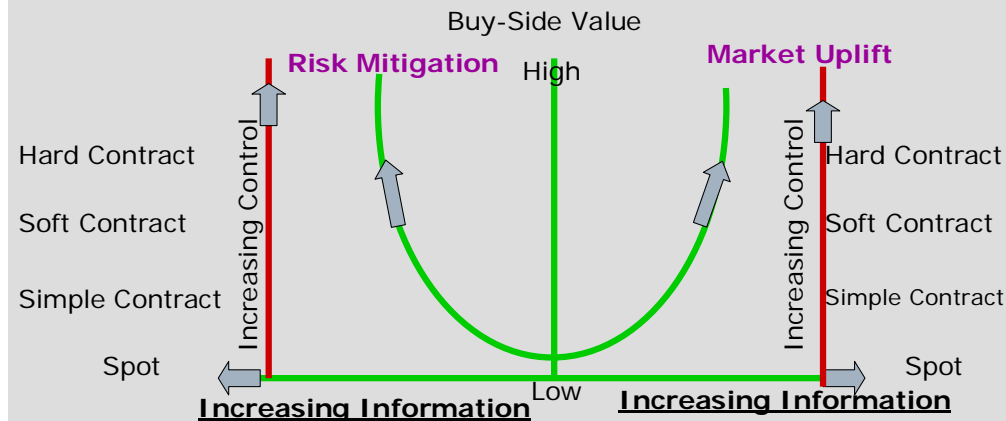
The Buy-side “Half-Pipe” – the buyer’s calculus

- Does the buyer really want a “relationship”?
 - Very little evidence in the food system
 - Substitutability the norm

- Simplicity in Procurement-not complexity
 - Opportunity!!!
 - e.g. Disintermediation

- Wary of over-investment in relationships
 - Low ROI
 - e.g. indemnification

Buy-Side Incentives for Supply Chain Control



Risk-Return and the Buyer's Calculus

□ Differing Procurement Systems

■ Specification Contract

□ Narrowly Defined

□ Strict Liability

■ Production Contract

□ Broadly Defined

■ Modified Spot

□ Pump Priming

□ Weakly Defined

■ Pure Spot

□ Undefined

- A. Increasing risk absorption by buyer
- B. Increasing complexity to procurement
- C. Increasing investment in procurement
- D. Increasing liability exposure*
- E. Decreasing substitutability
- F. Decreasing price competition
- G. Decreasing flexibility

What does the group do for these?

The Post-Modern Cooperative

- Needs to link the...
 - Neo-modernists (NGC/LLC movement)
- And
 - Industrial Marketing
 - Supply Chain Management
 - Relationship Marketing
 - The Wholesaling Function

9 Key Steps (1-5)

1. Build the business backwards, start with buyers' needs
 - Assemble resources to make buyer more competitive
 - See where group fits in.
2. Become the buyer's agent not the seller's agent
 - Understand customer needs
 - Spend time with end-users
 - <http://www.marketmaker.uiuc.edu/>
 - Address buyer's risk management
 - What is being done about indemnification?
 - Disintermediate costs/functions out of the system
3. Act as 1
 - Org. Design
 - Know what you grow (IT)
 - www.grainqualitytechnology.org
4. Access Working K- build reputation and support product
 - Knocking someone else off
 - Be Incremental- prove yourself

9 Key Steps (5-9)

5. Access and compensate the appropriate competencies
 - Access and integrate a variety of resources
6. Control and Value Intangible Assets
 - ROIA vs ROA
7. Offer Scale- it matters
8. Offer Scope- it matters
 - Bundle product/service/knowledge
9. Recognize we are in the S&G business
 - Not cost-based pricing
 - A “low price ceiling”

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