

Enhancing Farm Income Through Value Added Agriculture

By
Thomas L. Sporleder,
Ronald L. Overmyer,
and
Jeffrey D. Layman

Agriculture has been a rapidly changing industry for many years. Farmers understand that commodity prices over time reflect the cost of production with little margin. In fact, the latest U.S. Department of Agriculture statistics indicate that only 20 cents of every dollar consumers spend for food reaches the farm gate. The remaining 80 cents goes for adding value in processing, marketing, distribution, and retailing.

Can farmers participate in gaining some share of the 80 cents that currently goes elsewhere? Of course the answer is yes. Some farmers, particularly through farmer cooperatives, already participate in value added processing and capture some value added margin for themselves. Outstanding examples of this include Goldkist with poultry and Land 'O Lakes with dairy.

Value added activities are ones that add value to a product or service from the buyers' perspective. The forms of utility, or usefulness to buyers, include transforming commodities into other forms, such as processing wheat into flour. Another source of utility is time utility, such as storing. Yet another form of added value is from place utility, such as transporting commodities or products to locations where the price is higher. So, a broad set of activities adds value by improving the usefulness of the commodity or product to the customer.

Examples range from the simplest activity, such as feeding corn to hogs, to more complex processing such as manufacturing biodegradable plastics from corn. Leading examples of processing include manufacturing ethanol from corn or soydiesel from soybean oil. In addition farmers' markets and roadside stands add value to commodities in the time and place dimensions, without much further processing.

Market forces have contributed to better opportunities for product differentiation and added value to raw commodities because of 1) increased consumer demands regarding health, nutrition, and convenience; 2) efforts by food processors to improve their productivity; and 3) technological advances in everything from information systems, such as precision agriculture, to genetic technology that allows producing specialized commodities for targeted end use

¹ Thomas L. Sporleder is Professor of Agribusiness and Farm Income Enhancement Endowed Chair, Department of Agricultural, Environmental, and Development Economics, The Ohio State University; Ronald D. Overmyer is Coordinator of the Agricultural Business Enhancement Center of The Ohio State University Extension, Bowling Green, Ohio; and Jeffrey D. Layman is Extension Agent in Value Added Agriculture, The Ohio State University Extension, Columbus, Ohio.

markets. The combined effect of the technologies is that they help farmers more accurately produce what consumers and processors desire.

Commodity producers will continue to absorb all the shocks arising from global markets. Value added producers think of themselves as producing products for end users, instead of producing only raw commodities. For example, beef producers banded together in a concerted effort to produce genetically similar table-ready meat of consistent quality rather than simply producing finished (slaughter-ready) animals of uncertain genetics.

Often a value added strategy requires farmers to make significant off-farm investment. The investment may range from owning physical plant and equipment for processing to more subtle business expenditures, such as advertising a value added product or service. For farmers the economic decision always involves evaluating the trade off for any investment dollar between expanding farm operations or participating in value added activities off-farm.

Primary motivations for farmers to invest in value added activities include enhancing income or reducing the variability of income (e.g. processing a perishable commodity so it can be stored). Participating financially in value added activities would not necessarily increase commodity price for what the farmer sells. Rather, income enhancement is expected through the return on investment made in the additional value added business, not an increase in the commodity price. In fact, further processing operations typically strive to keep input cost as low as possible.

Some new assistance is available to farmers interested in participating in value added activities. Heartland Agdeavor Association (HAA), a non-profit corporation, began operation in September 2001. HAA assists in the development of value added ideas so they become viable businesses and helps farmers invest in the value added businesses of others. HAA offers four services for members: 1) networking with others that have similar interests, 2) intensively evaluating the most worthy ideas, 3) for the worthiest ideas providing feasibility studies to determine their economic viability, and 4) putting together business plans based on the best feasibility studies. The business plan step is part of the process for obtaining funding for a start-up business.

The value of membership in Heartland includes the right, but not the obligation, to invest in agriculture-related value added business start-ups of others. The potential for diversification of farmers' portfolios is improved through participation in HAA. The purpose of HAA over the long haul is to reduce the risk of start-up businesses in value added agriculture. Members have the opportunity of investing in a wide array of new ventures over time.

Membership for farmers costs \$200 in annual dues with an initiation fee of \$800 payable over three yearly installments. Partners and affiliates are other classes of members. Partners include the commodity organizations such as corn growers and pork council, and the general farm organizations such as the Ohio Farm Bureau. Partners also may be for-profit agribusiness corporations such as ADM and Cargill. Affiliates include primarily non-profit organizations such as the Ohio Department of Agriculture and The Ohio State University.

Farmers must cope with global commodity markets that influence their

economic well-being. Increasingly there is a need for customized production of commodities that serve specialized end use markets. This need translates into a new business opportunity for farmers. Through HAA farmers can participate in value added businesses that are harmonizing to their existing operations. Visit Heartland Agdeavor's Web site at: www.heartlandagdeavor.com or phone 614-818-4466 for more information. There are "Frequently Asked Questions" posted on the Heartland Web site that offer detailed information on almost every operational aspect of Heartland.