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# Cargill foresees new grain era

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A deceptive calm blankets the world's grain markets. For four years in a row, good weather has blessed American farmers and many of their counterparts elsewhere with bumper crops, bringing a leveling-off in the trading of wheat, corn, soybeans and other grains.

Yet at its headquarters just outside Minneapolis, Cargill Inc., the nation's largest privately owned company and the world's biggest grain trader, is quietly but aggressively preparing for a brand-new era. For Cargill, the next few years may be every bit as turbulent as the period following the 1972 Russian wheat deal that brought a boom in worldwide grain trading, a spectacular bulge in the profits of Cargill and other traders and unwelcome publicity for a business that is still shrouded in secrecy.

Now, another round of explosive growth in grain trading could be in the offing, accompanied by substantial new risks that are forcing Cargill to plan for a boom that might just as easily turn into a painful bust.

Three forces are at work that promise not only great opportunity but also uncertainty and turmoil for Cargill: A projected swelling of world demand for grains, a raft of new competitors and a threat of more stringent government controls. Although Cargill executives refuse to divulge their plans for dealing with such new developments, interviews with industry executives, analysts and former Cargill managers—supported by some of the company's recent moves—reveal a unique approach-avoidance strategy that Cargill is now taking toward its traditional business.

## Investment, protection

On one hand, the company is investing more heavily than ever in grain-handling and transport facilities at home and abroad to position itself for the widely predicted surge in trading. At the same time, however, Cargill is protecting itself against the added risks in trading by pursuing an equally vigorous program of diversifying away from it.

For fiscal 1979, ending June 1, fully half of the company's projected sales of \$12.6 billion and about 60 percent of its predicted \$150 million in profits will come from Cargill's rapidly growing non-trading activities. By contrast, in 1970, nearly 60 percent of the company's revenues were generated by Cargill's grain-trading operations. Even back then, Cargill had already diversified into such fields as corn milling, animal feeds, chemicals, salt mining, soybean processing and insurance.

But the company has since used its hefty grain-trading profits to expand those businesses and enter new ones, including flour processing, steel manufacturing, poultry processing and coal. In November, Cargill's desire for such diversification was underscored by the company's \$75 million acquisition of MBPXL Corp., the nation's No. 2 meatpacker (after Iowa Beef Processors Inc.) with annual revenues of about \$1 billion.

Despite such diversification, Cargill's biggest growth opportunities are still in the grain-trading business that it dominates with a 25 percent share of U.S. exports. (Continental Grain Co. of New York is next with about 20 percent.) The volume of worldwide trading today is 70 percent higher than in 1970, but the larger part of that growth took place during the first half of the decade, when Cargill's profits grew sevenfold, to more than \$200 million.

## Margins slashed

While worldwide grain demand has been growing at an annual rate of 10 percent since then, an unprecedented string of good crop years has leveled off the growth in trading and cut grain traders' margins drastically. Moreover, there are more than 1 billion bushels of U.S. wheat and feed grains in storage, a level that approaches the record government-supported surpluses of the 1960s.

The expected long-term grain boom rests partly on the law of averages, which deems another succession of splendid crop years extremely unlikely. Yet, for myriad economic and political reasons, the world demand for grain is predicted to grow even faster in the years ahead. The developing nations are gaining buying clout. The Soviet Union and Eastern-bloc countries are trying to put more meat in the diets of their populations, boosting their demand for feed grains.

And China has become the wild card in the global equation. Last month, China announced that it will make a number of big U.S. grain purchases this year. Noting such trends, some agriculture experts predict that grain-trading volumes could rise 50 percent in the next five years.

Anticipating this surge, several newcomers have recently jumped into the business to join the traditional Big Four—Cargill, Continental Grain, Bunge and Louis Dreyfus. Some of the corporate entrants, such as Peavey Co. and Pillsbury Co., are actually returning to a familiar field. They fled the industry in years past, seeking more profitable investments elsewhere. Still others, such as Philipp

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Bros., the huge metals-trading arm of Engelhard Minerals & Chemicals Corp., are new to the business altogether, but view grain trading as a related area.

At the same time, big farm cooperatives, powerful Japanese trading companies and others are now trying to grab a greater stake in grain handling and trading.

## Specter of restraint

But the most ominous threat to its prosperity is the one it can do the least about—government. While rarely betraying a doubt publicly, industry executives privately express fears that their free-trading days may be numbered. The government has been restrained in regulating grain traders. Considering the shady practices of some traders during the early 1970s and the federal investigations that followed, "remarkably little regulation has resulted," admits Cargill's vice president of public affairs, William R. Pearce.

Another grain-trading boom could dramatically change that. The government and farmer groups have traditionally been distrustful of the secretive grain traders. That hostility increased after the revelations of short-weighting, bribery and other shenanigans at Gulf Coast grain elevators in recent years. (Cargill and Dreyfus were the only major traders untouched by the scandals.)

The companies will probably come under even greater fire if, as expected, grain prices rise as demand outstrips supply. In periods of climbing prices, the grain traders, acting as market-makers, can benefit tremendously by matching production in one country with deficits in another. If the companies' profits soar, charges that the traders are "profiteering" probably will reach a crescendo. As one Bunge Corp. executive glumly observes: "I see no way to keep the government out of the market if we go through another bout of exploding prices."

A number of legislative proposals are already before Congress that would put the government much deeper into Cargill's business. The most drastic of these is a bill introduced March 16 by Rep. Jim Weaver, D-Ore., which would establish a National Grain Board modeled after government units in Canada and Australia. The board would have the power to "barter, negotiate or approve all export sales of American grain."

## Grain market's OPEC

Because U.S. exports of wheat, corn, soybeans and other grains represent half of the world market, the proposed board would be to grain what the Organization of Petroleum Exporting Countries is to oil. Should such a bill pass, it would crimp the grain traders in their most profitable role—the market-making function—and limit them to the much smaller profits to be made from grain handling and storing.

The chances of the grain board bill passing this session are slim, but other, similar proposals are gaining favor. Some farmer groups and congressmen are pushing for an international government-to-government arrangement for managing prices, creating yet another threat to Cargill's trading profits.

A more imminent concern to the company is the legislative call for more extensive and faster reporting of grain sales. Following the uproar over the Russian wheat deal and the disruption it triggered in world wheat markets, the federal government in 1973 began requiring grain traders to report the terms of all large domestic grain trades to the Agriculture Department within 24 hours.

But Cargill and other traders mostly sidestepped the requirement by giving their foreign subsidiaries a more active part in worldwide trading. Now, Con-

gress is debating a proposal that would extend the reporting requirement to the companies' foreign arms as well. The industry fears that such a system could reduce its margins even further by giving grain sellers and buyers more current information on prices and supplies.

Cargill executives also see another danger in such rules. "They would just force foreign buyers who desire privacy in trading to (use) foreign-based companies and diminish U.S. exports," argues Robbin S. Johnson, an assistant vice president at Cargill.

It is in this tumultuous milieu that Cargill is charting its strategic course. The company's executives are characteristically tight-lipped about the plans being hatched at headquarters—a palatial, 64-room replica of a French chateau, sequestered in a sylvan, 250-acre estate. Neither Chairman Whitney MacMillan, whose great-grandfather Will Cargill founded the company in 1865, nor President M.D. McVay would consent to interviews with Business Week. A few other Cargill executives did talk, but only sparingly. "Our strategy is the only proprietary part of this business," one stressed. "The lead time we build, keeping our competitors in the dark, is a big edge."

## Expansion underway

Nevertheless, it seems increasingly clear to close observers that Cargill is first hoping to maintain or even increase its hegemony in grain trading. Cargill's 350 elevators, 500 barges, 5,000 rail cars and 14 ocean-going vessels give the company a big lead over second-place Continental in grain-handling and storage facilities. Now, according to industry executives, Cargill is spending at the annual rate of about \$150 million to expand its grain-handling capacity by 50 percent by 1984. One Dreyfus executive laments: "Cargill is spending at a rate that no one could hope to match."

A number of major expansion projects are on the drawing board or are under construction. Just a few weeks ago, Cargill announced plans to build a huge Great Lakes export elevator at Burns Harbor, Ind., to handle that area's burgeoning soybean crop. Construction recently began on another new elevator at Toledo, while large additions to existing facilities are also pegged for Duluth, Houston, Chicago and Norfolk, Va.

Meanwhile, the company is revamping many of its 115 country elevators—the first way station in the export pipeline, to which farmers bring their grain—to increase that network's capacity to load rail cars. Together, these initiatives could boost Cargill's share of U.S. grain exports to 35 percent, by some estimates.

Cargill is also strengthening its position in foreign markets, thus grabbing additional sources of supply as a buffer against any production dips in the United States. For instance, the company recently purchased a chain of country elevators in France, which is rapidly increasing its wheat exports. Argentina and Brazil are two other countries whose growing grain production and export activity have prompted Cargill investments.

In Canada, where the government's Wheat Board now controls all trading, Cargill bought 200 country elevators in 1974. And the company is now expanding its Canadian grain terminal facilities. Cargill is gambling that Canada's desire to capitalize on the new opportunity in world grain trade will lead it to permit the big private companies to share in the more profitable trading function. "We're counting on the Canadian system moving more toward free markets," says Walter B. Saunders, group vice president, who heads the company's world grain operations.

But the success of Cargill's efforts to expand its grain business ultimately rests on the continuing supe-

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riority of its far-flung trading operations handled by an affiliated company called Tradax. An elite unit that thrives on intelligence gathering, secrecy and discretion, Tradax peddles most of Cargill's exports.

The unit, owned 70 percent by Cargill and 30 percent by a consortium of Swiss banks, keeps a letter-box "headquarters" in tax-sheltered Panama. But the real headquarters of Tradax is a six-story building in Geneva that houses sophisticated telecommunications equipment as well as its team of high-priced, cosmopolitan currency experts, grain traders and shipping specialists.

## Consulted by CIA

By all accounts, Cargill's trading mavens are quick-witted and urbane graduates of the most prestigious schools. Indeed, they are so plugged into political changes, crop developments and currency movements in foreign countries that agents of the Central Intelligence Agency are said to meet with them regularly to pick the traders' brains.

Tradax enables Cargill to react quickly to developments in sensitive grain markets, an invaluable asset in a business where the volumes traded are large and the margins thin. N. Leonard Alderson, senior vice president of Tradax, acknowledges that "Tradax gives us a significant market advantage."

Others have tried to copy Cargill's success with Tradax, but failed so far. In 1974, for instance, Continental opened a centralized Geneva office. But according to trade sources, the company found that it could muster neither the management talent nor the money to support such an operation. It is now reportedly dismantling the operation.

The trading style at Cargill is conservative, hedging rather than speculating, which gives the company fewer windfalls but also fewer big setbacks. Even for Cargill, through, trading in the international markets has been difficult for the past two years. "Margins have been very poor," says Alderson. Last year, in fact, an estimated 70 percent of Cargill's earnings came from non-grain operations.

Nonetheless, grain markets are not expected to remain weak much longer. "The important question now is whether world supplies can possibly keep up with demand," says Carroll G. Brunthaver, vice president of Sparks Commodities Inc. and a former assistant Agriculture secretary.

## Adversaries move in

When the market turns, those who stand to gain most will be the traders close to U.S. grain sources, which account for half of world shipments. Cargill, of course, is first among these. But the recent evolution of the world's grain market has attracted a wave of foreign and domestic traders eager to carve out a share of the business.

The big Japanese trading companies, for instance, have been active in grain markets for years. But until recently, they were content to buy U.S. grains from private traders, such as Cargill. Now, Japanese companies, such as Mitsui & Co. and Mitsubishi Corp., are attempting to cut out the middlemen by purchasing elevators and other grain-handling facilities in the United States. For example, Mitsui jolted the industry last March when it outbid Pillsbury for the terminal and country elevators of bankrupt Cook Industries Inc.

Cargill also faces an army of new domestic adversaries. In addition to Philipp Bros., Pillsbury and Peavey, the list of new and newly aggressive competitors includes: Farmers Export Co., a trading venture founded in 1968 and backed by six farm cooperatives; a joint venture by German-based Alfred C. Toepfer and two U.S. co-ops, and Tradigrain Inc., a company composed mostly of former Cook traders.

Yet, if any of the old-line traders can comfortably weather the competitive onslaught, it is Cargill. Not only are its grain operations stronger, but it is also more diversified than its trading company peers. For more than two decades, Cargill has made investments outside grain, seeking a buffer against the capricious gyrations of its basic business.

Still, it was not until the mid-1970s that Cargill started making a series of big diversification moves. In all, the company has spent more than \$1 billion on non-grain operations since 1972, compared with roughly \$200 million during the previous decade. And the last grain boom bankrolled this campaign.

Even after the acquisition of MBPXL, Cargill still sports a war chest of more than \$500 million cash, thanks largely to those heady days in 1973-74. As a private company, it is naturally much easier for Cargill to hold on to that cash; the company pays out less than 2 percent of net income as dividends to its 33 shareholders, who are mostly members of the Cargill and MacMillan families.

Like its trading, Cargill's diversification program has been conservative. In fact, the company's processing, milling, poultry, beef and animal-feed operations are seen almost as integration steps—investments "to create markets for grain," according to Thomas C. Veblin, an agribusiness consultant with SRI International.

## Price is the weapon

Where Cargill will invest to broaden its stance further is uncertain. Yet, it seems unlikely that the company will stray very far from the commodity-marketing, bulk-handling fields it knows so well. As one former Cargill executive notes: "There are no marketing tricks over there. Everything is a commodity. The only weapon they know is price."

Moreover, the emphasis on diversification during the 1970s reflects the management transition taking place at Cargill. Until a few years ago, the company was dominated by officers from the trading side of the business, while the "processing and feed people were almost a lower caste," recalls one former executive. Now that is changing. The differences between the two camps are exemplified by the disparate backgrounds and experience of MacMillan and McVay.

Chairman MacMillan, 49, is a trader. After graduating from Yale, he worked his way up as a vegetable-oil merchant and later as a grain trader. McVay, on the other hand, is the first executive from the processing side of the business to reach the presidency. He is a livestock specialist, schooled at Kansas State University. McVay, 60, seems to embody the new wave of management at Cargill. It is more operations oriented and technically trained; some of its members are MBAs, and many were educated in the Midwest—contrasting sharply with the liberal arts graduates of Harvard and Yale picked in the 1950s and 1960s to become Cargill's elite coterie of grain traders.

In the recent moves at Cargill, outsiders see the ascendancy of the technical camp generally and McVay in particular. "McVay is the brains behind it all," says one Cargill alumnus. "He's the guy who is setting strategy now."

If that is so, it probably reflects the subtle shift in Cargill's long-term priorities away from grain trading and in favor of food processing and other businesses that the company has undertaken lately. The shift is clearly a timely one. For, while Cargill is now beefing up its trading operations, hoping to capitalize once again on that superiority in the coming few years, there seems to be a recognition within the company that its next grain bonanza—if it materializes at all—may be its last.