



The Center for Food and
**Agricultural
Business**
at Purdue University

CAB CS 07.2

**Excel Co-op:
Responding to Biofuels**

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March 2007

PURDUE
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This case was developed by Dr. Jay Akridge, director; Ms. Maud Roucan, research associate; Dr. Allan Gray, associate director for research; Dr. Mike Boehlje, professor, all in the Center for Food and Agricultural Business, Purdue University; and Mr. Christos Bitsanis, former M.S. student in the Department of Agricultural Economics at Purdue University. The authors would like to thank Mr. George Green, General Manager of Excel Cooperative, for permission to develop this case around issues facing the Excel organization. The research assistance of Mr. Ben Arjomandi, M.S. student in agricultural economics at Purdue University, is gratefully acknowledged.

EXCEL CO-OP: RESPONDING TO BIOFUELS

George Green, General Manager of Excel Cooperative, put down the telephone and glanced at the row of model vintage Chevrolet Corvettes which lined the top of a bookcase. He sighed to himself as he thought about the tremendous changes in agriculture since any ‘Vettes like those had tooled around Monticello, Indiana. George had just wrapped up a call with one of his board members about the possibility that a new 100 million gallon ethanol plant would be located in Reynolds, Indiana. Reynolds, only six miles from Excel headquarters in Monticello, Indiana, had been designated BioTown USA by Indiana Governor Mitch Daniels, and rumors about a new ethanol plant there had been circulating for months. George’s board member had just heard another rumor that an announcement was coming soon.

“Join the crowd,” George thought, with four ethanol plants already operating or under construction in or on the fringe of his market area, it was a literal biofuels frenzy in Central Indiana. George, his board, and his management team had been discussing how to respond to the rapid expansion of ethanol processing capacity in and around the ten county market area served by Excel for the past year. For a farmer-owned farm supply and grain marketing cooperative, where were the opportunities? Where were the challenges? How should his organization respond?

While taking a 1969 Corvette Mako Shark out for a spin sounded awfully tempting, George knew it was time to make some decisions.

Excel Cooperative

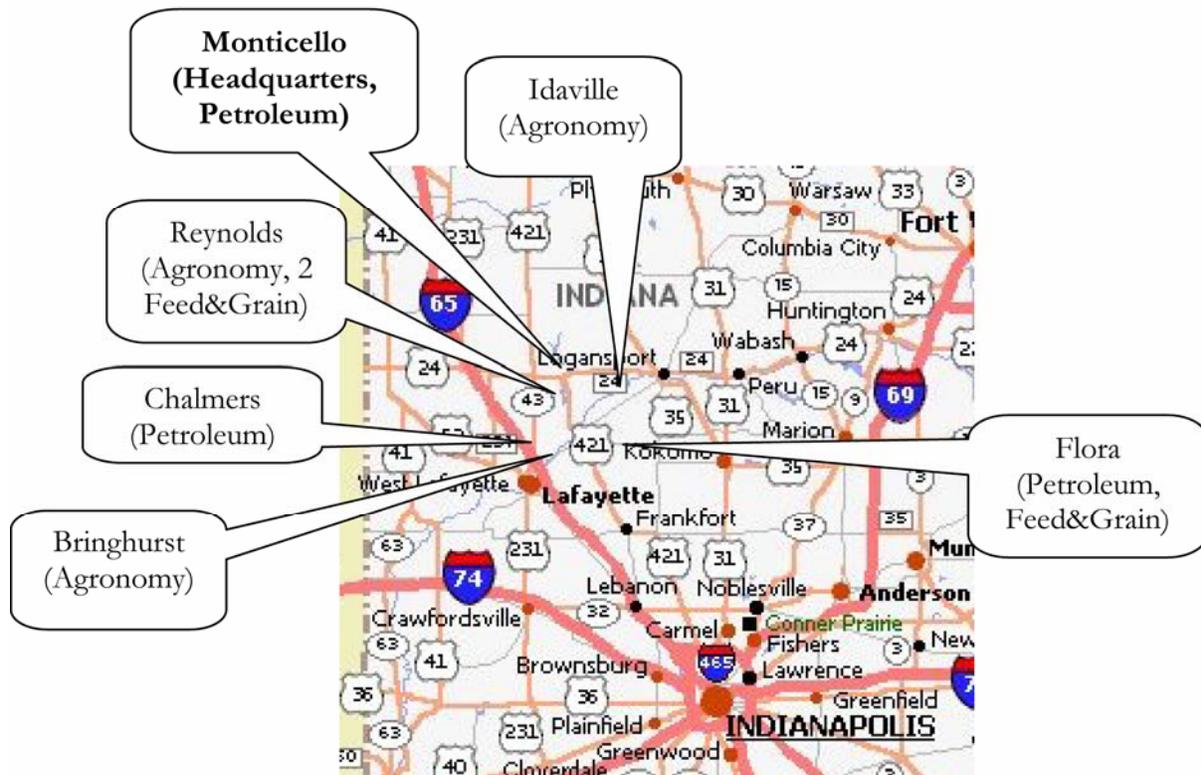
Excel Co-op is a member-owned farm supply and grain marketing cooperative serving farmers in north central Indiana (Figure 1). Corn and soybeans are the primary crops, and pork production is the primary livestock enterprise in this region. Excel was formed in 1995 when Carroll County Co-op merged with White County Co-op, and these two counties remain the organization’s most important markets. The cooperative is engaged in selling various farm supplies to local agricultural producers. Product lines include petroleum, fertilizers, crop protection chemicals, seed, animal feed, and other related supply items. The cooperative also has a pork production (livestock) division and is engaged in the contract production of hogs. In addition, Excel purchases and markets grain grown

by local producers. While the most important divisions of Excel Co-op are Agronomy (three locations), Energy (three locations), Grain (three locations), and Feed and Livestock (two feed mills), there are some smaller divisions/departments that provide technology services, lawn and garden products, and environmental, health, safety, and training services. The latter division focuses on providing other agribusinesses and farm organizations training and compliance consulting in these regulatory areas.

Excel Co-op has the following mission statement:

- Enhance profitability of the members and their cooperative
- Maximize resources to provide quality products and services at competitive prices
- Aggressively adapt to the changing needs of the agricultural community
- Adhere to sound and ethical practices

Figure 1. Map of Excel Cooperative Facility Locations



Source: Center for Food and Agricultural Business, Purdue University, 2007

General Trends in the Marketplace

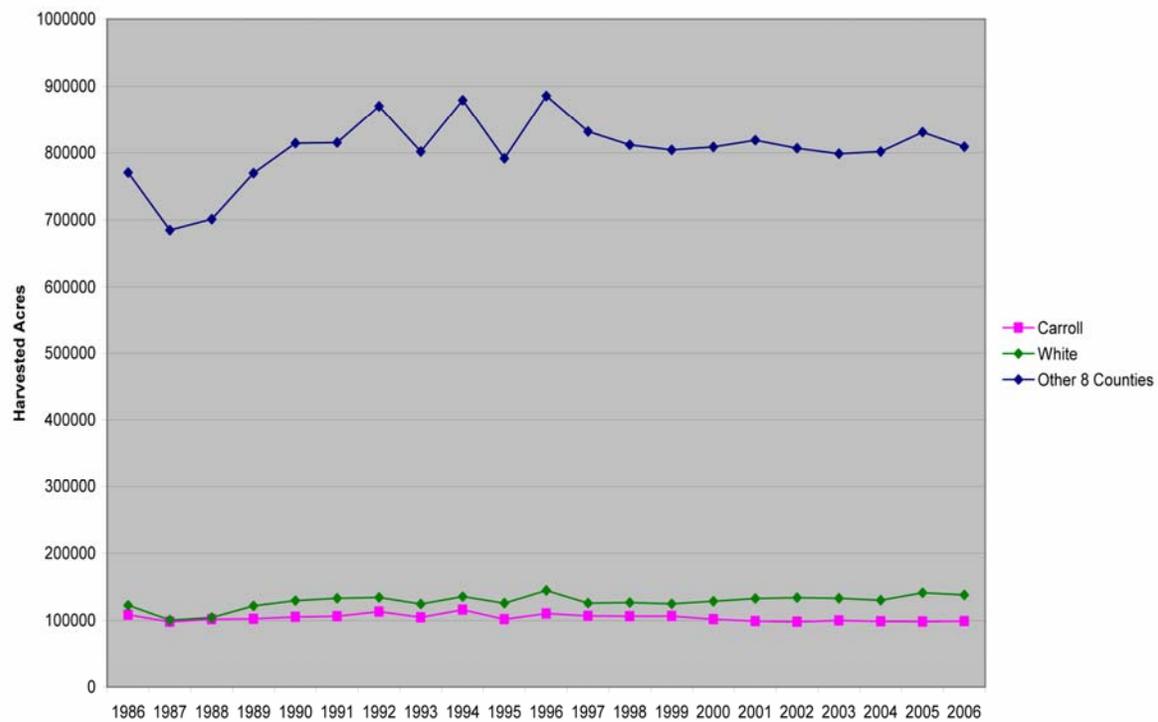
Globally, demand for corn is increasing due to major changes taking place in developing countries, especially in China and India. As income per capita increases in these countries, there is an increased demand for meat protein, which in turn increases demand for animal feed, in which corn is an important ingredient. In addition, a variety of political, economic, and social factors have combined to generate enormous interest in fuels from renewable feedstocks. In the U.S., this currently means ethanol from corn, and biodiesel from soybeans. At a state level, and perhaps responding to these global shifts, the newly formed (2005) Indiana State Department of Agriculture has articulated a strategy for expanding Indiana's food and agricultural sector that includes a dramatic increase in production of biofuels as well as doubling pork production. As a result of both sets of factors (feed and fuel), among others, demand conditions for corn over the next few years are projected to be exceptional.

Indiana is the nation's fifth largest corn producing state and fourth largest soybean producing state. In 2005, according to USDA, Indiana farmers marketed \$1.51 billion in corn, while soybean cash receipts were also \$1.5 billion, and receipts from the sale of hogs were \$770 million (USDA, 2006a). Indiana reported an inventory of about 3.25 million hogs in 2005 and corn farmers produced around 889 million bushels of corn and 263 million bushels of soybeans in that crop year (USDA, 2007a; USDA, 2007b). Of that 889 million bushel corn crop, about 20% was fed to livestock in the state, about 30% was processed into a variety of food and industrial products by mills and plants located in the state, and about 50% was shipped out of state, primarily to the pork and poultry markets of the southeast U.S., and for export to international markets.

Excel's market area touches a ten county region in north central Indiana. This region is characterized by intensive commodity agriculture and is home to some of the most productive soils in the state. The core of the Excel market area is White and Carroll counties. Since 2005, White County has been the leading corn producing county in Indiana (USDA, 2007c). Farmers in these two counties harvested about 237,000 acres of corn in 2006, some 39 million bushels (USDA, 2006b). Soybeans are the other major crop in the region, and in 2006 White and Carroll county farmers harvested about 197,000 acres of soybeans (10.6 million bushels) (USDA, 2006c).

For the ten county region, acreage dedicated to corn has been steady to slightly increasing since 1996, while acreage dedicated to soybeans has been trending lower (Figure 2, Figure 4). In 2006, farmers in the ten county region produced 171 million bushels of corn on just over 1 million acres (Figure 2, Figure 3) and 49 million bushels of soybeans on about 924,000 acres (Figures 4, Figure 5) (USDA, 2006b; USDA, 2006c). In 2006, before any (local) ethanol plants came on line, about 40% of this corn left the region, and was shipped via rail to the southeastern U.S. pork and poultry markets; about 35% of the corn was trucked to Lafayette, Indiana to feed one of the two massive Tate & Lyle corn processing plants located there; and the remainder was fed to livestock in the general area.

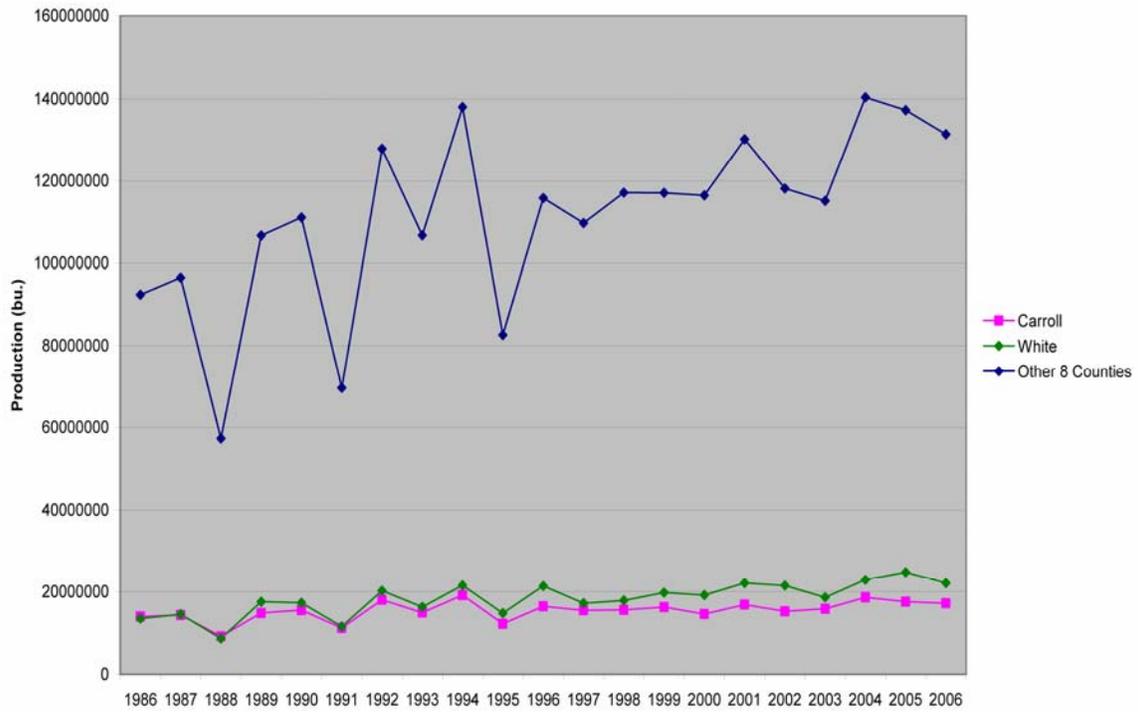
Figure 2. Acres of Corn Harvested in Excel's 10 County Market



*The Other 8 Counties are Benton, Cass, Clinton, Howard, Jasper, Pulaski, Tippecanoe, Tipton.

Source: USDA, National Agricultural Statistics Service.

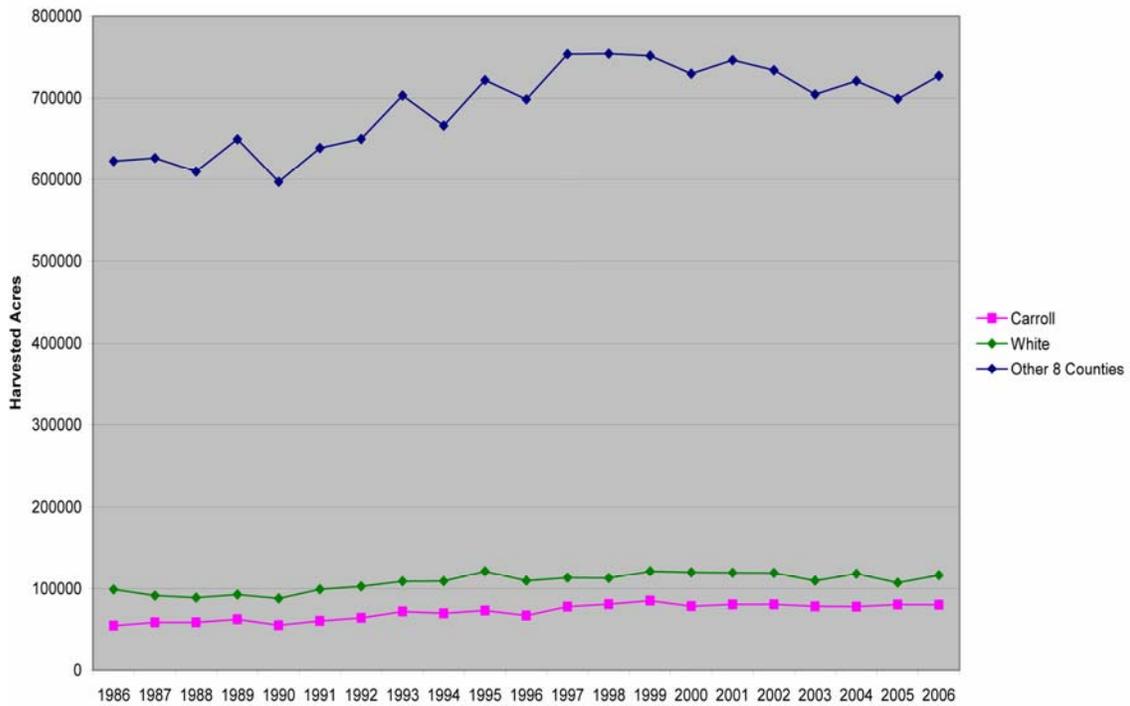
Figure 3. Bushels of Corn Produced in Excel's 10 County Market



*The Other 8 Counties are Benton, Cass, Clinton, Howard, Jasper, Pulaski, Tippecanoe, Tipton.

Source: USDA, National Agricultural Statistics Service.

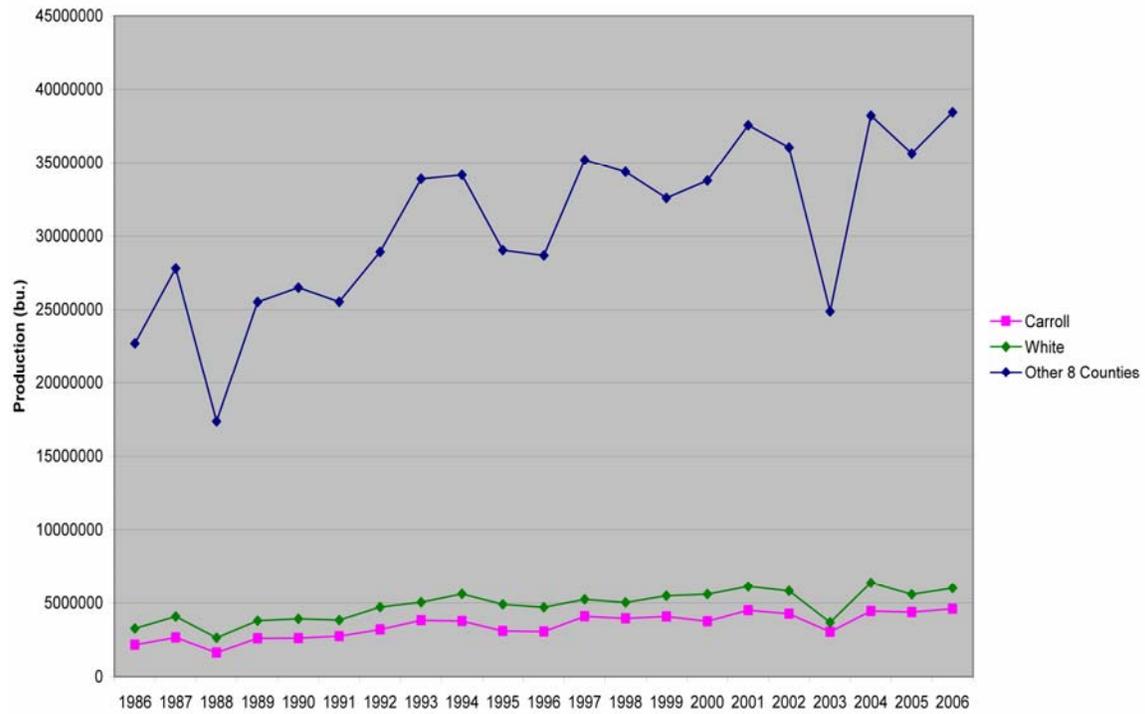
Figure 4. Acres of Soybeans Harvested in Excel's 10 County Market



*The Other 8 Counties are Benton, Cass, Clinton, Howard, Jasper, Pulaski, Tippecanoe, Tipton.

Source: USDA, National Agricultural Statistics Service.

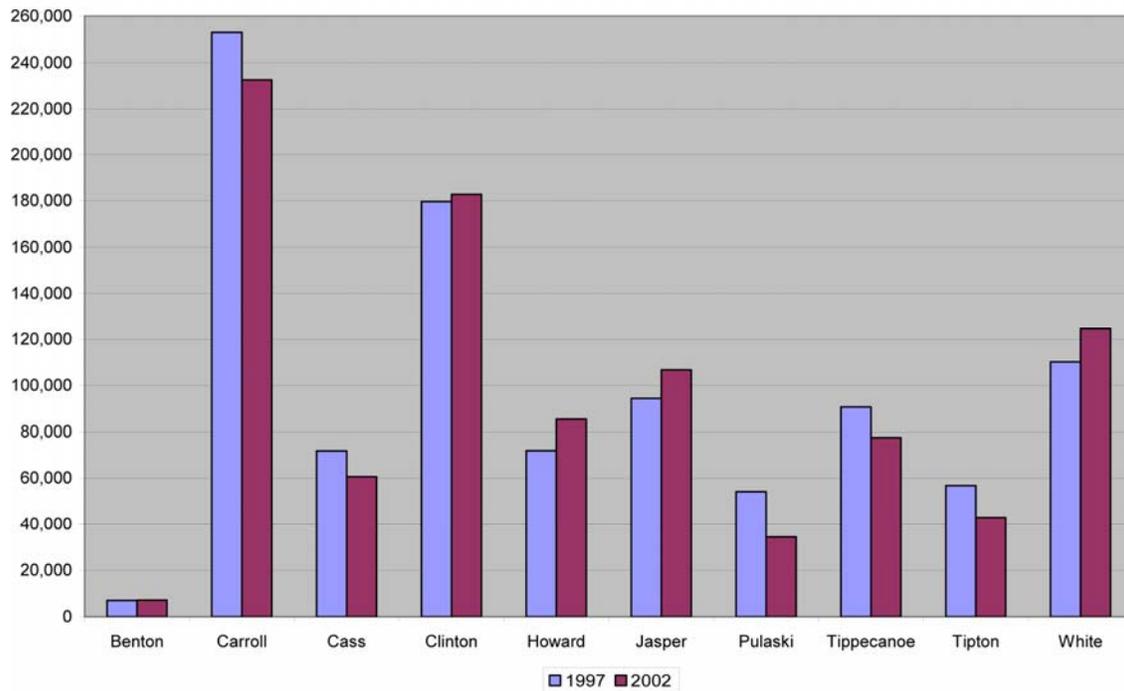
Figure 5. Bushels of Soybeans Produced in Excel's 10 County Market



*The Other 8 Counties are Benton, Cass, Clinton, Howard, Jasper, Pulaski, Tippecanoe, Tipton.

Source: USDA, National Agricultural Statistics Service.

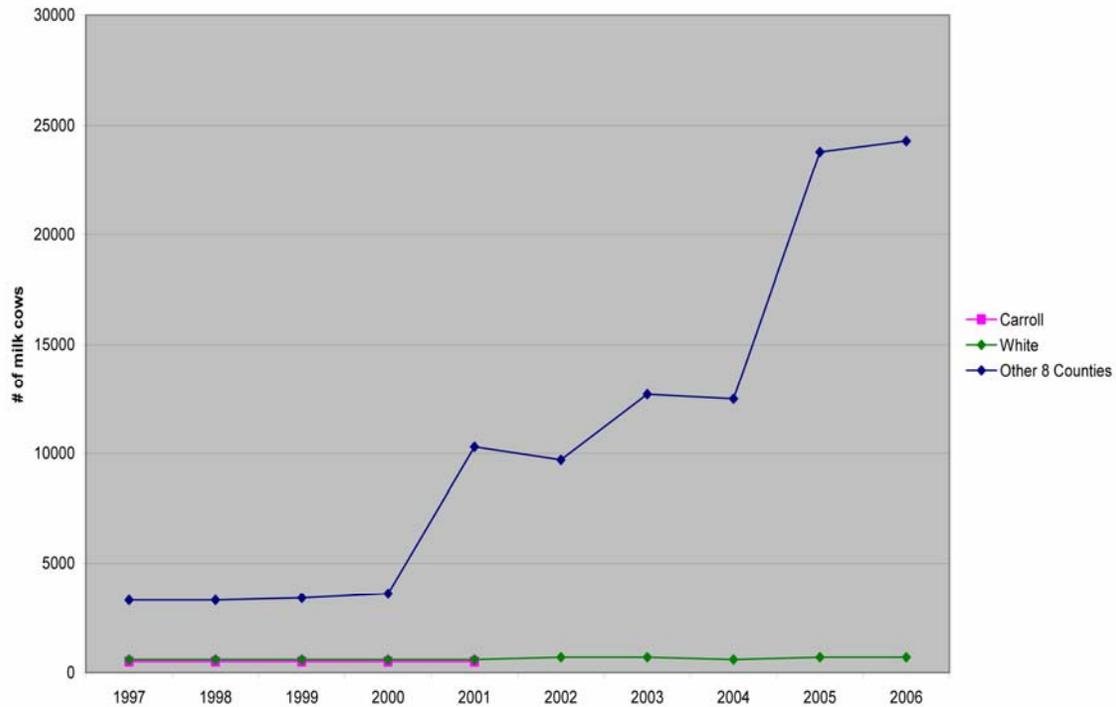
Figure 6. Number of Head of Hogs in Inventory in Excel's 10 County Market



Source: USDA, 2002a.

Data on county-level hog numbers is limited, with the last available data from 2002. In that year, the ten county region surrounding Excel marketed about 1.82 million hogs, and reported an inventory of 990 thousand animals (Figure 6) (USDA, 2002). The ten county area also reported more than 25,000 dairy cows on farms in 2006 (Figure 7) (USDA, 2006d).

Figure 7. Number of Head of Dairy Cows in Excel's 10 County Market



*The Other 8 Counties are Benton, Cass, Clinton, Howard, Jasper, Pulaski, Tippecanoe, Tipton. The total is understated as some individual counties cannot report data to protect confidentiality of respondents.

Source: USDA, National Agricultural Statistics Service.

Agronomy Division

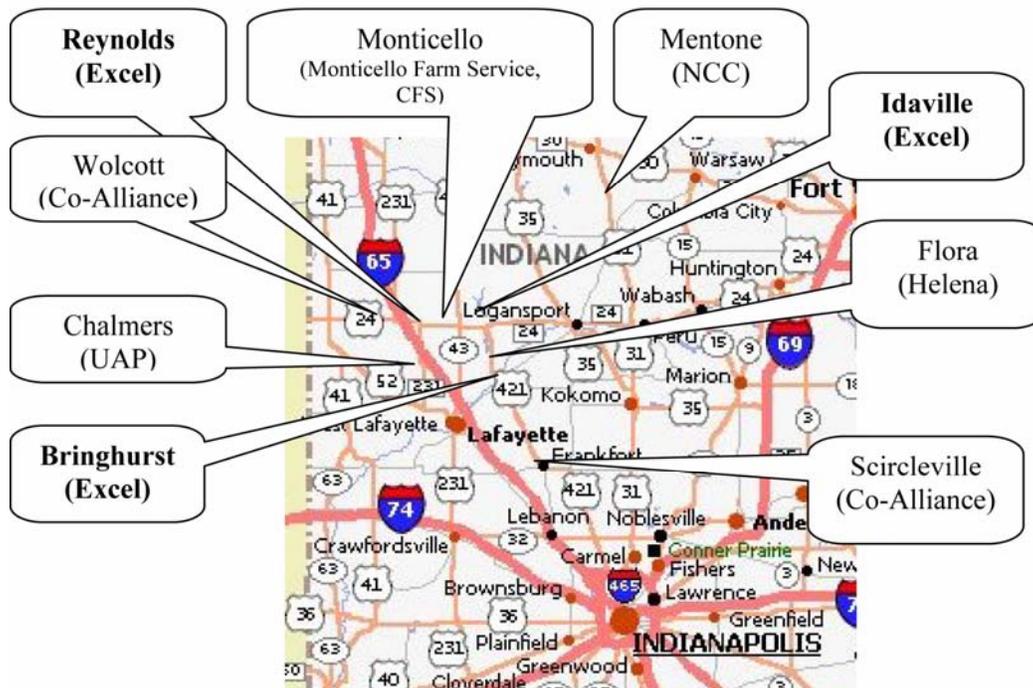
The Agronomy Division of Excel Co-op has three locations, in Bringhurst, Idaville, and Reynolds, and offers a complete line of crop production inputs to area growers: herbicides, insecticides, fungicides; custom application of liquid and dry fertilizers and chemicals; soil sampling; and corn, soybean, wheat, and legume seeds. Precision or site specific services such as soil sampling with GIS and variable rate application (VRT) of fertilizer and lime are offered by Excel, but the organization is still evaluating their overall approach to this area, hence revenue and profit contributions from precision services are still modest. Competition in the Excel market is intense because there is overcapacity in

the area and product margins have been eroding. This situation is due in part to biotechnology advances and seed varieties with ‘input traits’ which require lower levels of (and lower cost) pesticides and herbicides.

Overall, Excel sales of plant nutrients have been relatively steady in recent years, with some minor ‘shuffling’ of accounts between Excel and competitors. Crop protection chemical volumes and margins have declined with rapid adoption of glyphosate tolerant seed. More than 90% of the soybeans and 65% (and growing) of the corn in the region is glyphosate tolerant. Custom application revenues have held up, however there has been a significant shift from pre-emerge to post emerge application. Looking longer term, George is well aware that the additional corn acres driven by growth in biofuel production could be a real boost for his agronomy business. In fiscal 2006, Agronomy Division sales were \$16.9 million, accounting for 19% of total Excel sales, including 41,590 tons of fertilizers. The Agronomy Division represented 10% of the cooperative’s net operating income in fiscal 2006.

Competitors include independent organizations and branches of national crop input retailers in the Central Indiana area (Figure 8). In addition, Excel also faces competition from neighboring farmer-owned cooperatives. However, Excel is the market leader in White County, where it has a market share of about 50%. One of Excel’s major competitors is United Agri Products (UAP) located in Chalmers, Indiana. This location, a branch of a large, national company, is aggressively trying to expand. UAP has been through ownership changes in recent years. In the process, they closed a branch located between Delphi and Monticello, attempting to move sales from this branch to the Chalmers facility. While a full service operation, they have been aggressive with price in an attempt to build market share. UAP has two other facilities located on the fringe of the Excel market.

Figure 8. Map of Excel's Agronomy Locations and its Competitors



Source: Center for Food and Agricultural Business, Purdue University, 2007

Other strong competitors are an independent organization (Monticello Farm Service), Crop Fertility Specialists (CFS), and Helena. Monticello Farm Service recently had a change of management, and now has an aggressive new individual at the helm. There are a total of three CFS locations in or around the Excel market, each a full-service provider of crop production inputs. Likewise, another national chain, Helena, operates a facility near Flora. While many agronomy plants have changed hands over the past few years, almost all of the plants have remained open as the new owners choose to operate the facilities instead of reducing capacity in the region.

Competition from neighboring cooperatives is also important. Co-Alliance, a large, rapidly expanding central Indiana cooperative, has a facility in Wolcott and serves the market area south and east of Excel. In addition, Co-Alliance and the smaller Frontier Cooperative (which serves Boone and Clinton counties, also south of Excel) are merging, and this has created some disruptions in the market. Co-Alliance has a 40,000 ton 'hub' plant in Scircleville. These very large 'hub' facilities focus on lowering service cost through scale economies and efficient coordination of logistics over a much larger

service area than that covered by a traditional agronomy plant. North Central Cooperative (NCC), another large, rapidly expanding cooperative is a competitor to the north. NCC also has a 40,000 ton hub plant located in Mentone.

Energy Division

The Energy Division has two branches (in Chalmers and Flora) and offers farm and home delivery of diesel fuel, LP gas, and gasoline. Excel opened a new bulk petroleum facility in Chalmers in 2006 which replaced old bulk facilities in Chalmers and Monticello. The new bulk facility is state of the art and complies with all new state and federal guidelines for petroleum handling and storage. While Excel is closing a bulk facility in Monticello, they are building an unmanned card control facility on a busy street in the town, both to capture retail purchases of fuel and to serve several trucking firms located in the area. The new facility will be open in Spring 2007. In Flora, they also have a retail petroleum station, operated in partnership with a local entrepreneur. The firm offers E10 (10% ethanol, 90% gasoline) throughout their facilities and will be offering E85 (85% ethanol, 15% gasoline) at the new retail facility in Monticello. In addition, they offer B2 (2% biodiesel, 98% diesel) diesel through all of their facilities.

For fiscal 2006, the Energy Division's sales were \$24.6 million, 28% of total Excel sales. Total gasoline sales for fiscal 2005 were over 2.5 million gallons, total road diesel sales were around 2.5 million gallons, DX – four sales were 2.6 million gallons, heating oil sales were 404,000 gallons, and total LP sales were nearly 2.5 million gallons. Net operating income from the Energy Division represented 30% of the total in fiscal 2006. Excel holds more than 80% of the market in liquid fuels for on-farm use in its trade territory, and has very strong presence in bulk commercial fuels. They hope the investment they are making in new facilities will expand their share of the retail fuel business.

Grain Division

Excel Co-op's Grain Division has three locations. Two facilities are located in Reynolds (White County). The Reynolds-North location has 2.0 million bushels of grain storage, while the Reynolds-South location has 1.6 million bushels of grain storage. A major upgrade at the Reynolds-South facility in 2003 greatly enhanced the shipping options for Excel and now the two Reynolds locations can ship 65 or 90 rail car loads on the CSX Railroad, and 25 rail car loads on the TPW Railroad. This

\$850,000 project had a five year payout, is hitting all the numbers, and will be fully paid off in 2008. The Reynolds-South facility also has a 130 ton/day feed manufacturing plant (part of the Feed and Livestock Division) and sells livestock, horse and pet feed, and equipment. The grain department at Reynolds-South employs two grain merchandisers that assist farmers in the marketing of their grain.

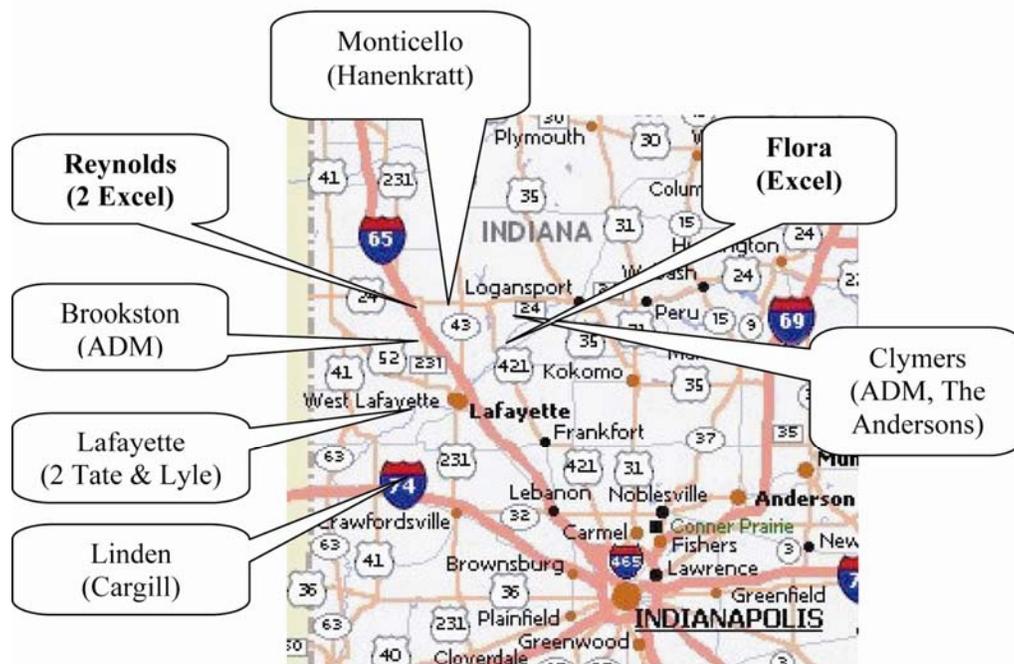
The other Excel grain facility is located in Flora (Carroll County) and has 1.3 million bushels of grain storage capacity. The Flora location also has a 150 ton/day feed manufacturing plant (again, part of the Feed and Livestock Division), as well as a country store and warehouse. The country store has a unique drive-thru loading area for easy pick-up of bagged feed, pet food, salt, lawn fertilizer, and grass seed. In addition, there is also a greenhouse to serve spring and fall garden needs.

Excel owns a total 4.9 million bushels of grain storage and is currently adding another 700,000 bushel storage facility at its Reynolds-South location. George is considering adding additional storage capacity to the Reynolds-South location – they have land available for another 2.0 to 2.3 million bushels of commercial grain storage. While the first 700,000 bushel expansion cost about \$2.2 million, each additional 700,000 bushel storage bin will run about \$1.0 to \$1.5 million. In general, George figures that commercial storage, with all needed support equipment, will cost about \$2 per bushel. Thinking through additional expansion at Reynolds-South, George knows he has other factors to consider besides storage capacity. Speed of unloading, traffic flow, and convenience may become even more important points of difference with area farmers as ethanol plants come on line. And, addressing these areas may require additional investment.

In total, Excel markets between 10 and 11 million bushels of grain each year – about 2.0 to 2.5 million bushels of soybeans, and the rest corn. In fiscal 2006, grain accounted for 35% of the cooperative's sales volume and 23% of its net operating income. Currently, most of its grain is shipped to the states of North and South Carolina and Georgia in 65 car trains, where it is primarily used as hog and poultry feed. The other major market is Lafayette, Indiana for the two Tate & Lyle corn processing plants.

Excel Co-op has two large competitors and several smaller ones that compete for grain in their market territory (Figure 9). Archer Daniels Midland (ADM) has a facility located in Brookston. This facility is 50% owned by Gold-Kist, a major southeastern poultry integrator. The ADM/Gold-Kist facility has about 2.5 million bushels of storage and can ship 65 car trains. Gold Kist invested in this facility in part to help them lock-up grain supply, anticipating that when the new ethanol plants come on-line, corn demand will be very high in the area and finding adequate supply of corn for its operations might be difficult. ADM also has a 3 million bushel storage facility in Clymers, which they own.

Figure 9. Map of Excel's Grain Locations and its Competitors



Source: Center for Food and Agricultural Business, Purdue University, 2007.

The Andersons, a diversified agribusiness firm that is an important regional grain and crop input organization, owns another 6 million bushels of grain storage in Clymers. About 50% of this is flat and upright storage that they constructed and about 50% is storage obtained when they purchased an old processing facility formerly owned by Bunge.

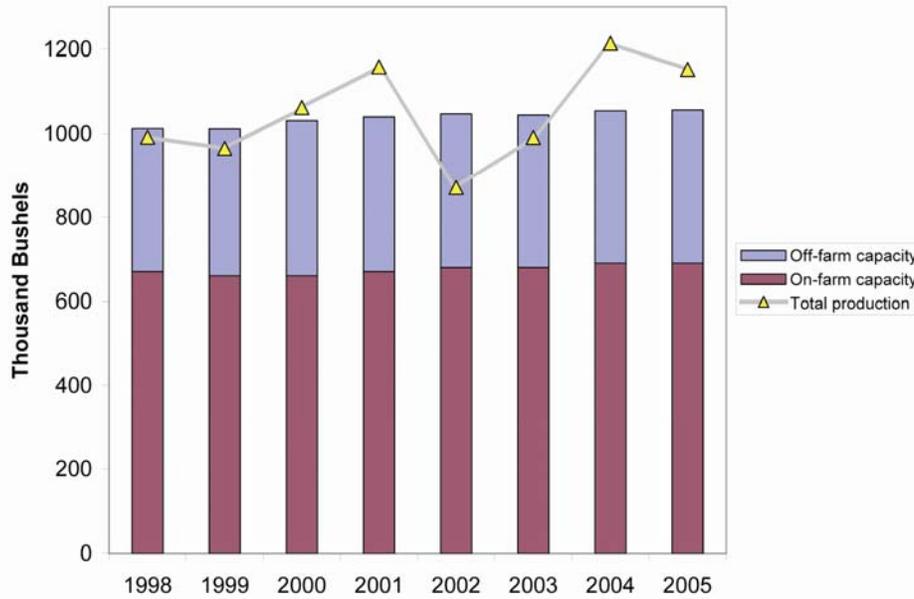
There is also an independent grain dealer, Hanenkrott Grain Co, based in Monticello. This is a small niche elevator that basically serves as a transportation firm. They have 10 to 15 semi trucks providing hauling services for farmers. Hanenkrott has very modest grain storage capacity.

Cargill's nearest facility is south of Excel in Linden. It is a large, 3.3 million bushel facility (USDA, 2007d). Recently, Cargill has been offering a program where they will build on-farm storage for ½ the commercial price, if the farmer will commit to marketing their grain with Cargill for three years. To date, grower interest in the program has been modest, as most growers are hesitant to commit to a market for their production for an extended period of time. However, George has wondered if there might be some potential for Excel to get involved with on-farm storage in some way. Such a 'condominium storage plan' might be an interesting approach to expanding Excel storage capacity, and an alternative (or complementary) to building more on-site storage.

Tate & Lyle, a multinational agricultural processor, owns two large corn processing plants in Lafayette. These plants process in excess of 95 million bushels of corn annually into high fructose corn syrup and other products from corn. Corn for these plants comes almost exclusively from Indiana, most from a 75 mile radius of Lafayette, and the plants represent a major corn market in Central Indiana.

In addition to commercial storage, farmer-owned storage is an important source of storage capacity in the area. Statewide, about 65% of Indiana's total grain storage capacity is located on farms (Figure 10).

Figure 10. Indiana Total Grain Storage Capacity: On-Farm and Commercial, 1998-2005.



Source: USDA, 2006e.

Feed and Livestock Division

Excel Co-op works with individual pork producers in the contract production of hogs, producing 75,000 hogs annually. In addition, Excel mills produce feed for another 125,000 hogs. Some 2.0 to 2.5 million bushels of corn is fed to these animals annually. The cooperative has two contract nursery sites and numerous contract finishing facilities. They purchase weaner pigs from two independent producers and then transport them to their contract nursery facilities. Excel makes about 60,000 tons of feed annually through its two mills located in Reynolds and Flora, with the amount split roughly equally between the two.

While growth has slowed, the pork production business does continue to expand in the Excel trade area as integrators look for low cost sources of corn, and to take advantage of the two large pork processing facilities in Logansport (Tyson) and Delphi (Indiana Packers). The cooperative has invested in facility upgrades over time and with a second shift, George figures he can double his feed mill capacity if needed. For fiscal 2006, feed sales and sales of hogs (the firm rolls these two areas together in its financial statements) accounted for 18% of Excel's sales volume and 37% of its net operating income.

Its biggest competitor in pork production is Hog Slat/TDN Farms, located in Flora. TDN contracts hogs all over Northern Indiana and feeds a total of about 200,000 hogs annually. United Feeds, a regional feed company headquartered in Sheridan, Indiana continues to serve the area. In addition, there are two farmer/integrators that have feed milling capacity and feed about 125,000 hogs annually. In total, there are at least 650,000 hogs in the area, and each hog will consume about 12 bushels of corn before heading to market.

Other Divisions/Departments/Units

Excel's Technology Services Division focuses on computer system applications in small and medium-sized agribusinesses. The division provides a wide range of services, from PC troubleshooting to ISO 9000 business consulting and web design.

The Environmental Health, Safety, and Training Department offers on-site, hands-on training, off-site classroom sessions, and electronic access to programs tailored to client needs in the health and safety areas. In addition to training, this department assists with the development and implementation of safety and compliance policies and procedures. A wide variety of training and consulting services are offered in areas such as hazardous communications/MSDS and personal protective equipment, Worker Protection Standard, pesticides (Core Training, RT Training, etc.), anhydrous ammonia safety, and DOT drivers' school (classroom).

The Flora Lawn and Garden Center offers a wide range of home and garden supplies and a variety of ornamental plants. It also has a greenhouse which is popular with local gardeners.

Combined, these divisions/departments/units represent less than 1% of total Excel sales, but account for about 2.5% of the cooperative's net operating income. While relatively modest in terms of overall contribution, business in these areas has helped diversify the organization a bit, as well as help the cooperative turn cost centers into profit centers.

Management and Organizational Structure

George Green, General Manager of Excel, is a lifelong Indiana resident and comes from a family with deep ties to agriculture. His father, Dr. Joe Green, was a veterinarian who served as Head State Veterinarian of Indiana for several years. From his position as State Veterinarian, Dr. Green guided the legislation that created the Purdue University School of Veterinary Medicine. Following graduation from Indiana State University, George began his agribusiness career as a feed salesman. In 1982 he assumed his first management role as General Manager of the Kosciusko County Farm Bureau Co-op. In 1984 he became Manager of Carroll County Farm Bureau Co-op which would later become part of Excel Co-op. He was appointed General Manager of Excel Co-op at the time of the merger which formed Excel in 1996. He continued his education while serving as Excel Co-op's General Manager and in December 2004 he received an MBA in Food and Agribusiness from the Krannert Graduate School of Management at Purdue University.

Individuals on Excel's ten member board of directors are each elected to serve three year terms. Six of the board members represent a specific geographic district, and four are at-large members. Only four of the ten current board members remain from the original board formed in 1996 at the time of the merger. George feels good about the 'new faces' and the overall quality of the cooperative's board.

In terms of organizational structure, George has one divisional manager. This person is responsible for the Agronomy Division and all three agronomy locations report to him. In addition, Excel has a Feed Marketing Manager to whom all feed sales representatives report to. In addition to these two individuals, all of the other facility and division managers and the CFO report directly to George. In total, Excel has about 100 full-time employees and adds another 25 employees during peak periods in spring and fall. George feels very good about the depth of his talent pool and the experience they bring to their jobs – many are in their 40s and have 20 or more years of experience under their belts. At the same time, he has some concerns about the next generation of management talent at Excel and wonders if he has enough 'young tigers' in the employee pipeline.

Excel Financial Performance

The cooperative generated around \$91.3 million in sales in fiscal 2006, of which \$57.3 million came from supply sales, \$30.1 million came from marketing activities, and \$3.9 million was service revenue (grain processing, custom application fees, feed grinding, shelling and weighing). The Excel board has issued a broad charge to George that the cooperative is to remain relatively balanced across the four core businesses of agronomy, energy, grain, and feed and livestock. Excel's net income for fiscal 2006 was \$2.5 million, up from \$2.0 million in 2005, and a significant increase compared to 2004's net income of \$63,000. Their operating profit margin for 2006 was 2.96%, about the same as 2005 at 3.33%, and compared to 0.79% in 2004. Asset turns were 2.49 in 2006, while 2005 asset turnover ratio was 2.76. The firm's debt-to-asset ratio for 2006 was 0.64, virtually unchanged from 2005, while in 2004 it was 0.62. Excel's current ratio in 2006 was 1.19, compared to 1.17 in 2005, and 1.15 in 2004.

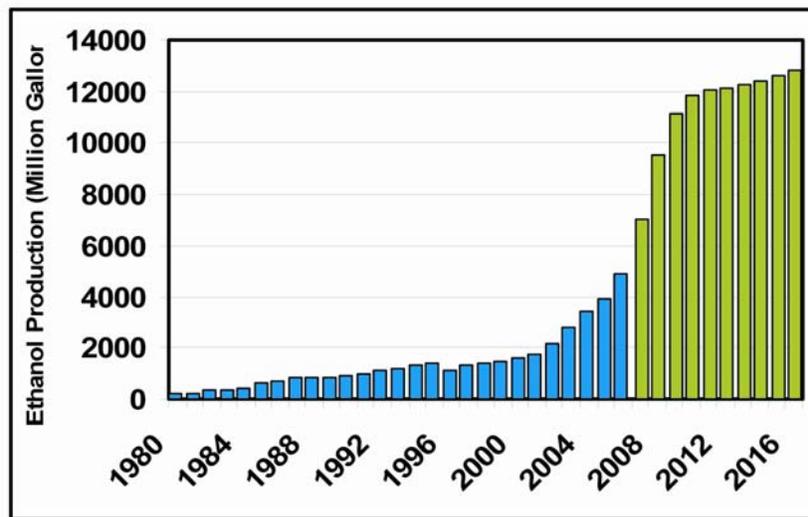
Excel has been a strong performer in recent years. In fiscal 2005 and 2006, the organization posted the highest return on patron investment (more than 20%) reported by cooperatives in the Indiana, Michigan, and Ohio region.

THE U.S. ETHANOL BOOM

The enactment of the nationwide Renewable Fuels Standard (RFS) was a historic commitment by the U.S. to renewable fuels such as ethanol and biodiesel. With the creation of a relatively secure future for continued growth in the demand for fuel ethanol and as gasoline prices have remained persistently high, U.S. ethanol production has increased dramatically. Ethanol production in 2006 reached the record amount of 4.9 billion gallons, an increase of 25% from 2005, and up 300% since 2000. The Energy Policy Act (EPACT) of 2005 requires the U.S. to produce 7.5 billion gallons of ethanol by 2012, which represents almost a doubling of the domestic ethanol industry in the next six years (Renewable Fuels Association). However, given actual and planned construction of ethanol plants, total production is expected to exceed this mandated figure (Figure 11). At the end of 2006, 73 ethanol refineries were being added to the existing 110 refineries, with an additional annual capacity of around 1.5 billion gallons coming on line when the refineries under construction are operational (Renewable Fuels Association, 2006).

There are a number of reasons for the boom in ethanol. First, was the boost provided by the Energy Policy Act of 2005. In addition, the American Jobs Creation Act of 2004 extended a \$0.51 per gallon tax credit for ethanol used in gasoline. Ethanol received another boost in May 2006 when liability protection was eliminated for petroleum firms using MTBE as an oxygenate in their fuel. Ethanol is the primary alternative to MTBE as an oxygenate, and demand for ethanol jumped as a result of the regulatory change. Finally, there have been substantial improvements in the efficiency of ethanol production. Between 1995 and 2005 the amount of ethanol that can be obtained from a bushel of corn has increased from 2.3 gallons to 2.8 gallons.

Figure 11. Ethanol Production and Forecasts, 1980-2016.



Source: RFA, FAPRI's U.S. Baseline Briefing Book.

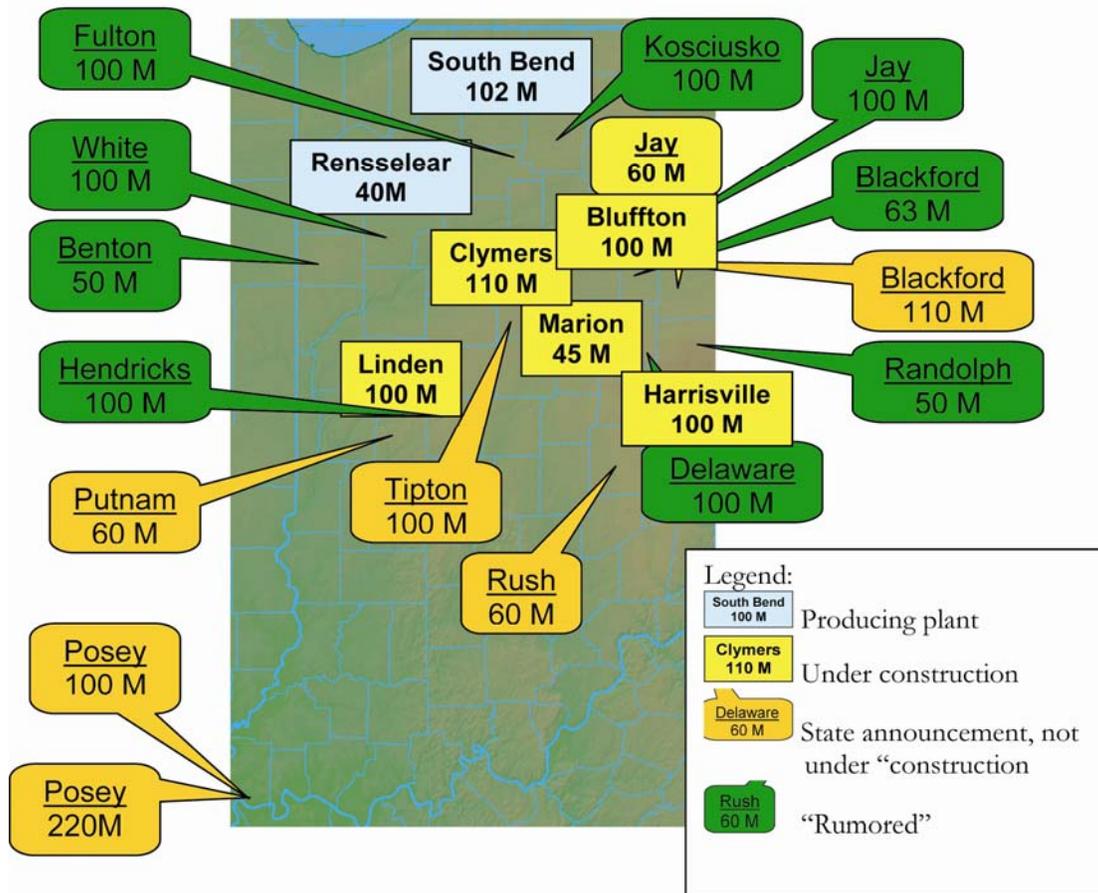
While it has its critics, ethanol is widely viewed as an environmental friendly energy source. It is also renewable and supporters argue ethanol can help the U.S. reduce its dependence on foreign oil imports. However, the basic reason for the increased interest in ethanol production is that the combination of high oil prices, modest corn prices, and federal and state incentives have made ethanol plants very profitable. As recently as fall 2006, an ethanol plant could pay back the initial investment in the plant in less than one year.

The Ethanol Situation in Indiana

The bulk of ethanol production capacity in the United States is located in the Upper Midwest and Western Corn Belt, with the combined capacity in Iowa, Nebraska, Minnesota, South Dakota and Illinois accounting for 80% of current production. Indiana historically has not been a major producer of ethanol, having only a single plant operating in early 2006 that supplied about 2% of the nation's total production. This plant, located in South Bend has a current ethanol capacity of 102 million gallons per year and processes about 38 million bushels of corn annually. A second plant capable of producing 40 million gallons of ethanol annually opened in fall of 2006 in Rensselaer. And, as of February 25, 2007, Indiana had six additional ethanol refineries under construction (Table 1, Figure 12). These eight total facilities either operating or under construction have a combined capacity of 657 million gallons of ethanol using 244 million bushels of corn, which is about 29% of 2006 Indiana corn production (844 million bushels). Six additional construction and expansion projects have been announced, and if these are completed, additional ethanol capacity of 650 million gallons requiring another 240 million bushels of corn would be created. Once operating, these 14 total refineries would require 57% of the 2006 Indiana corn crop.

However, 13 more refineries are in the 'rumor' stage, representing *another* 1.11 million gallons of ethanol capacity (412 million bushels of corn). The totals for those plants operating, under construction, announced, or rumored: 27 plants producing 2.42 billion gallons of ethanol requiring 896 million bushels of corn, or 106% of 2006 Indiana corn production. (In addition, three biodiesel facilities have also been proposed, with a combined annual capacity of 90 million gallons.) As mentioned earlier, 2005 data for Indiana corn movement show that out of 889 million bushels of corn produced in that year, 19% was used as animal feed in state, 29% was processed in state, and 52% was exported, primarily to the Southeast. Growing ethanol demand will change this corn utilization pattern dramatically

Figure 12. Location of Indiana Ethanol Plants, Partial Listing February 2007



Source: Center for Food and Agricultural Business, Purdue University, 2007

There are several possible consequences of the boom in Indiana ethanol production. First, corn prices are likely to increase and as a result of the increased demand for corn, acres will increase, while there will likely be a reduction in soybean and wheat acreage. According to George Green, if an ethanol plant is built in an area, the corn basis will narrow by 10-15 cents in a 50-60 mile radius, making corn production more profitable. In addition, it is quite possible that there will be a change in crop rotations, with a shift towards more continuous corn in central and northern Indiana. Current forecasts are for an increase in corn acreage of 8% to 10% nationally in 2007.

Table 1. Indiana's Current and Proposed Ethanol Production Facilities – February 2007

Ethanol Plants	Plant	Town	Capacity (million gal)	Corn Usage (million bu)
Operating Plant	New Energy Corp.	South Bend/St. Joseph	102	38
	Iroquois Bio-Energy Company, LLC	Rensselaer/Jasper	40	15
Under Construction	AS Alliances Biofuels, LLC-Cargill	Linden/Montgomery	100	37
	Central Indiana Ethanol, LLC	Marion/Grant	45	17
	The Andersons Clymers Ethanol, LLC	Clymers/Cass	110	41
	Premier Ethanol, LLC (Broin Companies)	Portland/Jay	60	22
	Cardinal Ethanol	Harrisville/Randolph	100	37
	Indiana Bio-Energy, LLC	Bluffton/Wells	100	37
State Announcement -Working with ISDA	Altra Indiana, LLC	Cloverdale/Putnam	60	22
	Rush Renewable Energy, LLC	Rushville/Rush	60	22
	AS Alliances Biofuels, LLC-Cargill	Tipton/Tipton	100	37
	Central States Enterprises, Inc.	Montpelier/Blackford	110	41
	AS Alliances Biofuels, LLC-Cargill	Mt. Vernon/Posey	100	37
	CGB, Inc./Aventine Renewable Energy	Mt. Vernon/Posey	220	81
Considering to Rumored	Hartford Energy LLC	Hartford City/Blackford	63	23
	Indiana Ethanol, LLC	/Randolph	50	19
	VeraSun Energy	Reynolds/White	100	37
	Maize AgriProducts	Fowler/Benton	50	19
	Louis Dreyfus Group	Claypool/Kosciusko	100	37
	The Andersons, Inc.	Dunkirk/Jay	100	37
	Indiana Renewable Fuels, LLC	Near "County Line Landfill"/Fulton	100	37
	Morning State Energy	Pittsboro/Hendricks	100	37
	U.S. Ethanol Holdings, LLC	Muncie/Delaware	100	37
	Vieste LLC	Lafontaine/Wabash	88	33
	NuFuels LLC	Huntington	100	37
	Hoosier Ethanol	/Dekalb	60	22
	American Milling Company	Millford/Kosciusko	100	37

Source: Renewable Fuels Association (2006b)/Purdue University (2006)

Less certain is what will happen to soybean prices, since they will be stimulated by smaller acreage and greater demand for biodiesel, but at the same time depressed by the widespread availability of an ethanol co-product, a feed ingredient called Distiller's Dried Grains with Solubles (DDGS), and reduced soy crushing.

Moreover, since ethanol plants don't usually store grain for more than ten days, but need to operate year round, more grain storage space will likely be needed. Since more corn will be needed for local ethanol plants, the volume of corn and soybeans exported from Indiana ports will probably decline and rail traffic to Southeast hog and poultry market will likely decline, although there is a possibility that some DDGS will be exported to these markets.

DDGS

Distiller's Dried Grains with Solubles (DDGS) is a co-product of the distillery industries and 98% of the DDGS in North America come from plants that produce ethanol for oxygenated fuels, while the remaining 1 to 2% of DDGS is produced by the alcohol beverage industry. DDGS are used in livestock feeds and according to the USDA they can substitute for a portion of corn or soybean meal in animal rations. Its overall feed value varies by specie depending on the different capacity of the species to digest the product. The maximum inclusion rates in efficient rations are considerably higher for cattle and other ruminants than non-ruminants, and usually are about 35% for cattle on feed and 30% for dairy cows, compared to about 15% for hogs and 10% for broilers (Informa Economics).

Depending on ethanol and by-products prices, DDGS account for almost 15% of an ethanol plant's revenue. DDGS comprise about 32% of the corn input and this remains as a feed product from ethanol production process, so the feed industry in Indiana will change substantially after the additional ethanol plants come on-line. What will happen to the production of DDGS, given that it will probably exceed potential livestock use in the state? As a result of the likely supply-demand imbalance, Indiana DDGS could be exported to Pennsylvania, New York and other nearby eastern markets where large concentrations of dairy cattle are found. Another question is how will this potentially low cost feedstuff affect the number of hogs, poultry and cattle in Indiana?

EXCEL CO-OP AND ETHANOL

Given the quantity of corn produced in Excel's ten county market, it is no surprise that the area is a hotbed of ethanol activity. Four plants are operating, under construction, or planned, and George will not be surprised to hear the announcement for the fifth plant any day. A summary of the plants, and their grain procurement strategies follows.

Rensselaer: Iroquois Bio-Energy broke ground on a 40 million gallon, 44,000-square-foot, \$66 million, dry grind corn ethanol plant on September 1, 2005. The plant has about ten days of grain storage on-site. The firm has a contract with The Andersons to manage their grain origination and they are a minority equity investor in the facility. The refinery is capable of processing up to 15 million bushels of corn a year into 40 million gallons of fuel-grade ethanol. Privately held Iroquois Bio-Energy funded development of the plant using a combination of private funds and loans, along with \$6 million in grants from the U.S. Department of Energy.

Clymers: The Andersons is the largest equity investor in this 110 million gallon ethanol plant, which is expected to come on-line in the first quarter of 2007. This plant is located adjacent to a major (6 million bushel) Andersons grain storage facility in Clymers.

Linden: Demeter Enterprises broke ground on a 100 million gallon ethanol facility in January 2006. Demeter is an operating company owned by Cargill, ASAlliance Holdings, a subsidiary of a Dallas merchant bank, and Fagen, the construction firm which has built about 2/3 of all ethanol plants constructed in the U.S. over the past five years. Cargill has a major grain storage facility in Linden, and will be managing grain procurement for the plant.

Boswell: Maize Agriproducts is planning an 88 million gallon dry mill ethanol facility in Boswell, Indiana to produce fuel grade ethanol, distillers grains, and CO₂. Once complete, the state of the art dry mill plant will employ 40-45 employees, purchase over 32 million bushels of local corn, produce 88 million gallons of fuel grade ethanol, and 262,000 ton of DDGS annually. To this point, Maize Agriproducts has not yet formalized any relationships to originate their grain.

Reynolds: For months, rumors have been flying that VeraSun Energy would announce plans for a 100 million gallon ethanol plant in Reynolds. A number of activities in support of such an announcement have occurred, including rezoning a 250+ acre parcel north of Reynolds from agricultural to I-2, heavy industrial. This plant, if constructed, would have about ten days of grain storage on-site. As far as George knows, VeraSun Energy has not yet signed any grain procurement agreements.

Biofuels and the Agronomy Division

George wonders how the ethanol boom will affect his agronomy business. Clearly, growers will shift more land towards growing corn. The current allocation of planted acres between corn and soybeans is about 50-50, but this will probably change in favor of corn to 60-40 or perhaps even more. Corn requires more inputs than soybeans, and strong corn prices will encourage farmers to invest heavily to maximize yield. George fully expects his agronomy business to be at least 10-15% greater in 2007. How sustainable is this increase? What will it mean for his people and equipment resources? Can he service that type of increase through his existing infrastructure? How should he help prepare his growers for some of the agronomic challenges of continuous corn?

Biofuels and the Energy Division

Clearly, ethanol means transportation – transportation of massive amounts of grain to the plant, and transportation of massive quantities of ethanol and DDGS away from the plant. Much of this transportation will involve truck traffic. What opportunities exist for Excel in this area? They already have a thriving commercial fuel business, can they expand this with the increase in local transportation requirements? Should they consider entering the trucking business, and offer their services to the makers of biofuels?

Biofuels and the Grain Division

Excel Co-op buys around 9 million bushels of corn and 3 million bushels of soybeans in White and Carroll counties from farmers ranging in size from 600 to 8000 acres. The more corn it can control, the larger the cooperative's bargaining power will be. How will these giant ethanol processing plants with their huge need for corn change the local grain markets? Excel has the physical assets and stra-

tegic railroad location to export grain to the Southeast livestock markets. If the majority of the grain is needed locally, how can Excel best use its multimillion dollar grain handling facility? Are there opportunities to partner with Tate & Lyle, to take on a greater role in procuring grain for existing processors? If (as?) VeraSun Energy finalizes its plans, can Excel align themselves in some fashion with this new entrant, or with one of the other ethanol refiners without a grain origination partner?

Biofuels and the Feed and Livestock Division

George knows that Excel's Feed and Livestock Division also faces some important challenges. While the State of Indiana may want to double hog production, feeding hogs very high priced corn makes profits difficult to come by. Moreover, the introduction of DDGS also contributes to the uncertainty of the market and logistics will have to change. What can Excel do to maintain its profitability? What changes if any will it have to make with regard to its hog production? More broadly, what does this massive local demand for corn mean for Excel's feed business?

DECISIONS

George took a last look at his model Corvette collection before leaving his office. Yes, it was a radically different agriculture. How should he educate his employees about the upcoming changes to ensure they are prepared to be successful in this new environment? He has an experienced and dedicated workforce that knows the Central Indiana market and is a great fit with the co-op's culture. Do they possess the skill set to succeed in this rapidly changing environment?

More broadly, what is the role of a local grain and supply cooperative in this new agriculture that now serves the food, feed, and energy markets? Excel's board of directors believes in balance across the cooperative's four core businesses. Could such balance be pursued in light of the ethanol boom? And, even if it could, was it the right strategy for the organization? Each of Excel's four core divisions face a significant set of strategic opportunities and challenges. It seems that several essential questions—what role? which partners? what investments?—and the timing of all the answers to these questions were on the table at the same time.

A challenge, he thought – yes it was. He loved the old 'Vettes, and yet that 2008 Blue Devil Corvette with a 6.2L supercharged engine turning more than 650 horsepower he had been reading about in *Car and Driver* sure looked fun...

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Excel Co-op 2005 to 2006 – Management Structure

The Board of Directors

The Excel Co-op Board of Directors consists of 10 farmers from the Carroll and White County area. A combination district and at-large candidate system assures geographic balance and that areas of heavy business concentration are represented. All ten members are successful businessmen and are respected community leaders. Farm size ranges from 1,000 acres to 6,000 acres. While some have specialty crops such as popcorn or grow for seed companies most of the acres are in 60% commercial corn and 40% soybeans. Seven of the board members maintain an interest in pork production. Two own large sow herds and are local integrators with other farmers. Three own new finishing facilities and grow out pigs for regional integrators. Two of the members still own small farrow to finish operations but are considering changing to finish only operations. None are actually growers for Excel Co-op pigs.

The individual board members generally support the co-op with their purchases, though only a minority is 100% in all business lines. Energy is supported by all members. Most members purchase crop nutrients and crop protection from the co-op but the large farm members are very demanding in terms of price and service. None of the members buy a significant amount of seed from Excel. These issues carry over into the board room at times. The smaller independent feeders use the feed mills but the larger do not. Unfortunately the board has not totally disciplined itself in terms of competing activities. The two sow farms not only compete for local growers but both utilize their large farm feed mills to mix feed for other farmers. The grain division is utilized by most of the board members but only for a portion of their marketing.

Each board member has a high regard for the other members and they enjoy comparing farm notes before and after each meeting. Attendance is excellent and the board is very engaged. The Executive committee of the board is solid and there are two non officers to whom other board members defer to out of respect. This tendency to yield to one another sometimes leads to indecision but this is usually limited to smaller issues.

The Management Team

Overall the Excel Co-op management team is a nice blend of individuals averaging 45 to 50 years of age. As this would imply, they have several years of experience but still have many years left of highly productive service. As stated in the case, the overriding concern is that management team is not deep in terms of numbers. Each manager is frugal, hands on, and runs with minimal staff. They all work side by side with their employee groups. While this is appreciated by the employees it is also a concern for the company as these managers are not physically as young as their labor force. At some point age and management depth will become an issue. The management structure is flat with most location managers reporting directly to George Green. The CEO is the only individual that reports directly to the board.

Administration

George Green is supported by two key individuals in administration. Jeff Griffeth directs the accounting functions along with leading the IT department in both its internal activities and externally marketed functions. Jeff is a hard working individual early in his career with great potential for upper management. Jerry Hendress works in employee development and as a customer relationship manager. He is well known and well thought of in the community. He has a strong background in feed so he also coordinates the interaction between feed mills and the swine division managers.

Energy Department

Vince Seward and Greg Stockment split the Energy department management geographically east and west. They each have responsibility over bulk liquid fuel products and propane deliver. Each also has consumer retail outlets that they oversee. The two individuals are experienced and are generally thought of as two of the best in the state by their co-op associates. Both are courted regularly by competitors and by supply chain vendors. While either could likely handle the “whole” department, losing one to a nearby competitor would be very detrimental.

Feed, Grain, and Pork Production

The grain elevators and feed mills are integrated operations. They are managed at the two primary locations by Brad Stockment and Dale Orem. Each is solid veteran of the business and each runs a tight ship with a record of consistent profitability. They are also recognized locally as knowledgeable on grain marketing. Sam Moffitt manages the pork production and he is known in the industry for his knowledge. Each year he is invited to judge several county fairs. Pork production at Excel Co-op is very complex and is at a cost disadvantage to other integrated swine operations because several production units are old. However, Sam does an excellent job controlling cost factors.

Agronomy Department

The agronomy facilities are the only locations that do not report directly to the CEO. Dennis Turner is department manager, and is a veteran in the agronomy business having operations management experience at local co-ops and marketing management experience in the supply chain. The three locations are under a department manager to the coordinate people and equipment resources and to maximize purchasing power. Dennis is also positioned in part to be a mentor for the three location managers. Because the Agronomy team has undergone several changes in recent years, the location managers have high potential but they are early in their management careers. The location managers are John Loy, Jeff Ruemler and Scott Williams. Each has three years or less in their management role.

Environmental, Health, and Safety

Steve Salomon and Mike Titus are well known throughout the state as the best in their field. Steve is an excellent trainer and is well versed in regulatory issues. Mike is excellent as an emergency responder. Together they are a formidable team.

Excel Case Study – Discussion Questions

- What are the key threats and opportunities Excel Cooperative faces in its External environment?
 - Grain
 - Agronomy
 - Energy
 - Feed & Livestock

- What are the key success factors for Excel to thrive/survive in the market within and across divisions?

- What are Excel’s core competencies?

- What are the key issues facing Excel over the next 2 to 5 years?

- How should Excel respond to the changes taking place in their markets?

EXCEL CO-OP, INC.
FINANCIAL STATEMENTS
August 31, 2006 and 2005

EXCEL CO-OP, INC.
Monticello, Indiana

FINANCIAL STATEMENTS
August 31, 2006 and 2005

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Crowe Chizek and Company LLC
Member Horwath International

REPORT OF INDEPENDENT AUDITORS

Board of Directors
Excel Co-op, Inc.
Monticello, Indiana

We have audited the accompanying balance sheets of Excel Co-op, Inc. as of August 31, 2006 and 2005, and the related statements of operations, shareholders' and patrons' equity and cash flows for the years then ended. These financial statements are the responsibility of the Cooperative's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Excel Co-op, Inc. as of August 31, 2006 and 2005, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying schedules of operating expenses are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements taken as a whole.

Crowe Chizek and Company LLC
Crowe Chizek and Company LLC

Elkhart, Indiana
October 20, 2006

EXCEL CO-OP, INC.
BALANCE SHEETS
August 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
ASSETS		
Current assets		
Cash	\$ -	\$ 1,175
Advances and deposits	1,552,450	1,417,799
Receivables, net (Note 3)	6,367,113	5,754,767
Inventories (Note 4)	11,893,888	10,805,109
Deferred income taxes (Note 2)	510,400	350,000
Other current assets	<u>47,056</u>	<u>26,646</u>
Total current assets	20,370,907	18,355,496
Property and equipment - net (Note 5)	7,940,280	5,876,488
Other assets		
Investments (Note 6)	4,656,594	4,203,748
Notes receivable	-	265,097
Other	<u>78,259</u>	<u>104,009</u>
	<u>4,734,853</u>	<u>4,572,854</u>
	<u>\$ 33,046,040</u>	<u>\$ 28,804,838</u>
LIABILITIES, SHAREHOLDERS' AND PATRONS' EQUITY		
Current liabilities		
Checks in excess of bank balance	\$ 39,754	\$ 100,361
Accounts payable	1,525,970	1,517,919
Advances	21,187	241,384
Grain payable	686,136	671,448
Notes payable to bank (Note 7)	10,826,898	9,265,492
Current maturities of long-term debt (Note 8)	420,000	400,000
Customer deposits	904,065	536,186
Patronage payable	550,000	325,000
Other current liabilities	<u>2,009,964</u>	<u>2,595,602</u>
Total current liabilities	16,983,974	15,653,392
Deferred income taxes (Note 2)	776,000	619,500
Long-term debt (Note 8)	3,294,300	1,714,300
Pension liability (Note 10)	-	481,167
Other long-term liabilities	13,035	14,533
Shareholders' and Patrons' equity		
Preferred stock (Note 9)	55,275	57,775
Common stock (Note 9)	5,255	5,285
Patron equity credits	4,036,868	4,107,514
General reserve	6,296,494	4,761,486
Undistributed savings	1,759,539	1,678,553
Accumulated other comprehensive loss	<u>(174,700)</u>	<u>(288,667)</u>
	<u>11,978,731</u>	<u>10,321,946</u>
	<u>\$ 33,046,040</u>	<u>\$ 28,804,838</u>

See accompanying notes to financial statements.

EXCEL CO-OP, INC.
STATEMENTS OF OPERATIONS
Years ended August 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Sales		
Supply	\$ 53,835,130	\$ 49,617,127
Marketing	<u>28,635,461</u>	<u>30,121,933</u>
	82,470,591	79,739,060
 Cost of sales	 72,729,649	 69,827,645
 Gross margin on sales		
Supply	8,245,675	8,704,041
Marketing	<u>1,495,267</u>	<u>1,207,374</u>
	9,740,942	9,911,415
 Service revenue		
Grinding, shelling, and weighing	88,925	120,477
Plant food related income	1,052,639	962,865
Grain processing	990,971	881,375
Miscellaneous service revenue	<u>945,055</u>	<u>880,742</u>
	<u>3,077,590</u>	<u>2,845,459</u>
 Gross operating income	 12,818,532	 12,756,874
 Operating expenses		
Fixed facility	1,507,601	1,375,437
Employee cost	5,662,262	5,631,226
Other	<u>3,018,171</u>	<u>3,021,586</u>
	<u>10,188,034</u>	<u>10,028,249</u>
 Income before other revenue (expenses)	 2,630,498	 2,728,625
 Other revenue (expenses)		
Interest earned	208,374	188,914
Patronage refunds received	1,247,254	534,652
Interest expense	(1,119,896)	(743,273)
Other revenue	<u>6,921</u>	<u>80,419</u>
	<u>342,653</u>	<u>60,712</u>
 Savings before income taxes	 2,973,151	 2,789,337
 Provision for income taxes (Note 2)	 <u>660,903</u>	 <u>782,925</u>
 Net savings	 <u>\$ 2,312,248</u>	 <u>\$ 2,006,412</u>

See accompanying notes to financial statements.

EXCEL CO-OP, INC.
STATEMENTS OF SHAREHOLDERS' AND PATRONS' EQUITY
Years ended August 31, 2006 and 2005

	Comprehensive Income	Preferred Stock	Voting Common Stock	Patron Equity Credits	General Reserve	Undistributed Savings	Accumulated Other Comprehensive Income	Totals
Balance - September 1, 2004		\$ 58,675	\$ 5,345	\$ 4,171,207	\$ 4,701,535	\$ 60,046	\$ 13,140	\$ 9,009,948
Allocation of undistributed savings	-	-	-	-	60,046	(60,046)	-	-
Preferred stock dividend	-	-	-	-	-	(2,859)	-	(2,859)
Redemption of equity	(900)	-	(60)	(63,693)	(95)	-	-	(64,748)
Provision for cash patronage refunds	-	-	-	-	-	(325,000)	-	(325,000)
Net savings	-	-	-	-	-	2,006,412	-	2,006,412
Other comprehensive income	2,006,412	-	-	-	-	-	-	-
adjustments (net of tax benefit of \$192,500)	-	-	-	-	-	-	-	-
Unrealized gain on cash flow hedge	(13,140)	-	-	-	-	-	(13,140)	(13,140)
Minimum pension adjustment	(288,667)	-	-	-	-	-	(288,667)	(288,667)
Comprehensive income	<u>1,704,605</u>	-	-	-	-	-	<u>(288,667)</u>	<u>(288,667)</u>
Balance - August 31, 2005		57,775	5,285	4,107,514	4,761,486	1,678,553	(288,667)	10,321,946
Issuance of stock	-	-	110	-	-	-	-	110
Allocation of undistributed savings	-	-	-	290,641	1,422,269	(1,678,553)	-	34,357
Preferred stock dividend	-	-	-	-	-	(2,709)	-	(2,709)
Other adjustments	-	-	40	-	(40)	-	-	-
Transfers	-	-	(5)	(117,338)	117,343	-	-	-
Redemption of equity	-	(2,500)	(175)	(243,949)	(4,564)	-	-	(251,188)
Provision for cash patronage refunds	-	-	-	-	-	(550,000)	-	(550,000)
Net savings	-	-	-	-	-	2,312,248	-	2,312,248
Other comprehensive income	2,312,248	-	-	-	-	-	-	-
adjustments (net of tax expense of \$76,100)	-	-	-	-	-	-	-	-
Loss on cash flow hedge	(174,700)	-	-	-	-	-	(174,700)	(174,700)
Minimum pension adjustment	288,667	-	-	-	-	-	288,667	288,667
Comprehensive income	<u>2,426,215</u>	-	-	-	-	-	<u>(174,700)</u>	<u>2,426,215</u>
Balance - August 31, 2006		\$ 55,275	\$ 5,255	\$ 4,036,868	\$ 6,296,494	\$ 1,759,539	\$ (174,700)	\$ 11,978,731

See accompanying notes to financial statements.

EXCEL CO-OP, INC.
STATEMENTS OF CASH FLOWS
Years ended August 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Cash flows from operating activities		
Net savings	\$ 2,312,248	\$ 2,006,412
Adjustments to reconcile net savings to net cash from operating activities		
Depreciation and amortization	1,084,194	1,061,518
Unrealized loss on cash flow hedge	(174,700)	(13,140)
Minimum pension liability	-	(288,667)
Bad debt expense	-	20,977
Gain on sale of property and equipment	(195,486)	(58,114)
Deferred income taxes	(196,400)	(154,500)
Patronage refunds received in equity	(693,329)	(276,439)
Change in assets and liabilities		
Receivables	(347,249)	(861,630)
Advances and deposits	(134,651)	(1,185,533)
Inventories	(1,088,779)	(2,956,694)
Other assets	5,340	138,073
Accounts and grain payables	22,739	761,383
Customer deposits	367,879	110,467
Other liabilities	<u>(807,333)</u>	<u>1,299,609</u>
Net cash from operating activities	154,473	(396,278)
Cash flows from investing activities		
Purchase of property and equipment	(3,147,985)	(1,173,059)
Proceeds from sale of property and equipment	195,486	123,650
Purchase of investments	(13,219)	(13,119)
Proceeds from sale of investments	<u>253,701</u>	<u>59,654</u>
Net cash from investing activities	(2,712,017)	(1,002,874)
Cash flows from financing activities		
Checks in excess of bank balance	(60,607)	100,361
Net increase in notes payable to bank	1,561,406	1,731,013
Principal payments on long-term debt	(400,000)	(400,000)
Proceeds from long-term debt	2,000,000	-
Proceeds from sale of stock	110	-
Redemption of stock and equities	(251,188)	(64,748)
Preferred stock dividends	(2,709)	(2,859)
Patronage refunds	<u>(290,643)</u>	<u>-</u>
Net cash from financing activities	<u>2,556,369</u>	<u>1,363,767</u>
Net change in cash	(1,175)	(35,385)
Cash at beginning of year	<u>1,175</u>	<u>36,560</u>
Cash at end of year	<u>\$ -</u>	<u>\$ 1,175</u>
Supplemental disclosures of cash flow information		
Cash paid during the year for		
Interest	\$ 1,086,235	\$ 708,671
Income taxes	1,208,123	30,000

See accompanying notes to financial statements.

EXCEL CO-OP, INC.
NOTES TO FINANCIAL STATEMENTS
August 31, 2006 and 2005

NOTE 1 - NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES

Operations: Excel Co-op, Inc., is a member owned farm supply and marketing cooperative, based in Monticello, Indiana. The Cooperative is engaged in selling various farm supplies to local agricultural producers which include petroleum, plant food, chemicals, feed, and other related items. The Cooperative also purchases and markets grain grown by local producers.

Cash: The Cooperative maintains its cash primarily in one bank account which, at times, may exceed federally insured limits.

Accounts Receivable: The Cooperative accounts for trade receivables based on the amounts billed to customers. Past due receivables are determined based on contractual terms. The Cooperative accrues interest on all past due receivables. There were \$412,641 and \$278,943 at August 31, 2006 and 2005, of trade receivables past due 90 days or greater accruing interest.

Allowance for Doubtful Accounts: The allowance for doubtful accounts is determined by management based on the Cooperative's historical losses, specific customer circumstances and general economic conditions. Periodically, management reviews accounts receivable and records an allowance for specific customers based on current circumstances and charges off the receivable against the allowances when all attempts to collect the receivable have failed.

Inventories: Grain inventories are stated at market. The Cooperative hedges its grain inventories and unfilled contracts to the extent management considers necessary for minimizing risk from market price fluctuations. Unrealized hedging gains and losses on open futures and forward contracts are included in inventory and offset to cost of sales. Realized hedging gains and losses on closed grain futures and forward contracts are charged to current cost of sales. Agricultural supply inventories are stated at the lower of cost (first-in, first-out basis) or market.

The Cooperative operates in an environment where the value of its inventory and related contractual obligations are constantly subject to market price fluctuations, which at times can be significant. In order to minimize the risk of loss from market price fluctuations, the Cooperative hedges its grain and feed inventories and unfilled contracts to the extent management considers practical. Strategies employed by the Cooperative may at times include the use of derivatives in the form of forward or futures contracts as a tool to reduce this risk of loss. All derivatives are recorded at their fair value, with the offset being reflected in the cost of sales.

Reclassification: Certain prior year amounts have been reclassified to conform to the current year presentation.

EXCEL CO-OP, INC.
NOTES TO FINANCIAL STATEMENTS
August 31, 2006 and 2005

NOTE 1 - NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES

(Continued)

Property and Equipment and Depreciation: Property and equipment are recorded at cost. Expenditures that significantly extend the lives of assets and major improvements are capitalized. Depreciation is provided using the straight-line method for financial statement purposes over the estimated useful lives of the respective assets. Repairs and maintenance are charged to operating expenses as incurred.

Advances and Deposits: Advances and deposits represent uninsured deposits with a broker, and advances to vendors.

Investments: Investments consist primarily of investments in other cooperatives. The investments are valued at cost and adjusted annually for the Cooperative's share in their earnings based upon patron volume, net of equity distributions made in cash.

Patrons' Equity: In accordance with the provisions of the by-laws currently in effect, net savings arising from business done with or for members, reduced by the pro-rata share of dividends paid on preferred stock and general reserve additions, are distributed to the members as patronage refunds on the basis of the dollar volume of business transacted with them during the year through the functions that realized such net savings. A minimum of twenty percent of the patronage refunds is paid in cash, and the balance issued in qualified written notices of allocation (ownership equities) within (8-1/2) months after the close of the fiscal year. A provision for the estimated cash portion of the patronage refund is reflected in the financial statements as a current liability for years when a patronage refund distribution is anticipated.

Income Taxes: The Cooperative is organized and operates as a non-exempt agricultural cooperative. Accordingly, income distributed to patrons in the form of qualified patronage dividends is deductible by the Cooperative for income tax purposes. The Cooperative records income tax expense based on the amount of taxes due on its tax return plus deferred taxes computed based on the expected future tax consequences of temporary differences between the carrying amounts and tax bases of assets and liabilities, using enacted tax rates. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

Use of Estimates in the Preparation of Financial Statements: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Significant estimates made by the management of the Cooperative include the depreciable lives of property and equipment, the allowance for doubtful accounts and the estimated qualified patronage to be paid. Actual results could differ from those estimates.

EXCEL CO-OP, INC.
NOTES TO FINANCIAL STATEMENTS
August 31, 2006 and 2005

NOTE 1 - NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES

(Continued)

Concentration of Credit Risks: The Cooperative extends credit to customers, generally unsecured. The majority of these customers are engaged in the agribusiness industry in the general vicinity of Monticello, Indiana. The Cooperative's ability to collect these receivables is dependent, to some degree, on the economic conditions in the agribusiness sector within its market area.

Derivatives and Hedging: The Cooperative enters into swine futures transactions to hedge the sale price of future swine production. The Cooperative considers these transactions to be cash flow hedges of anticipated transactions and accounts for them as cash flow hedges under FAS 133. The Cooperative considers these transactions to be highly effective in hedging the proceeds of its sales and has accounted for these as having no ineffectiveness with respect to the current arrangements. The resulting gain or loss on open and closed futures contracts is included in other comprehensive income and will reverse into income when the related swine inventory is sold.

Comprehensive Income: Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes gains and/or losses relating to cash flow hedge arrangements and the minimum pension liability which are also recognized as a separate component of equity.

Fair Value of Financial Instruments: The carrying amounts reported in the Cooperative's balance sheet for notes receivable and debt at August 31, 2006 and 2005 approximates their fair values based on the current interest rate environment and the terms of the instruments. The Cooperative reflects derivatives in its financial statements at fair value. The Company's derivatives consist of grain forward and future contracts and hog future contracts and the fair values are detailed in Note 4.

NOTE 2 - INCOME TAXES

The provision for income taxes consists of the following:

	<u>2006</u>	<u>2005</u>
Current federal taxes	\$ 575,964	\$ 593,173
Current state taxes	164,939	151,752
Deferred income taxes	<u>(80,000)</u>	<u>38,000</u>
	<u>\$ 660,903</u>	<u>\$ 782,925</u>

EXCEL CO-OP, INC.
NOTES TO FINANCIAL STATEMENTS
August 31, 2006 and 2005

NOTE 2 - INCOME TAXES (Continued)

The deferred tax assets and liabilities are as follows:

	<u>2006</u>	<u>2005</u>
Deferred tax liabilities	\$ 824,000	\$ 849,000
Deferred tax assets	558,400	579,500

No valuation allowance was provided on deferred tax assets.

The deferred tax liabilities consist of temporary differences between the tax basis and financial reporting basis of property and equipment and temporary differences in reporting of nonallocated equity credits. The deferred tax assets consist primarily of temporary differences in reporting of accounts receivable and accrued pension.

NOTE 3 - RECEIVABLES

Receivables consist of the following:

	<u>2006</u>	<u>2005</u>
Accounts	\$ 4,935,422	\$ 4,643,965
Notes	262,505	113,054
Grain	661,648	520,634
Other	<u>873,067</u>	<u>850,265</u>
	6,732,642	6,127,918
Less allowance for doubtful accounts	<u>365,529</u>	<u>373,151</u>
	<u>\$ 6,367,113</u>	<u>\$ 5,754,767</u>

EXCEL CO-OP, INC.
NOTES TO FINANCIAL STATEMENTS
August 31, 2006 and 2005

NOTE 4 - INVENTORIES

Inventories consists of the following:

	<u>2006</u>	<u>2005</u>
Farm supplies		
Petroleum products	\$ 635,291	\$ 714,945
Plant food	4,333,489	3,787,591
Chemicals	1,889,417	1,266,652
Feed	128,256	138,693
Farm supplies	130,836	134,869
Hogs	2,814,402	3,063,177
Other farm supplies	<u>51,416</u>	<u>41,188</u>
	9,983,107	9,147,115
Grain		
Corn	1,568,126	1,537,368
Soybeans	513,266	121,184
Gain on forward contracts	123,580	276,261
Loss on forward contracts	(1,154,633)	(1,102,742)
Net gain on futures contracts	<u>860,442</u>	<u>825,923</u>
	<u>1,910,781</u>	<u>1,657,994</u>
	 <u>\$ 11,893,888</u>	 <u>\$ 10,805,109</u>

Inventory shown on the balance sheets at August 31, 2006 and 2005 does not include 163,562 and 133,878 bushels of grain, respectively, held in storage for others. The Cooperative is liable for any deficiencies of grade or shortage of quantity that may arise in connection with the above inventory held in storage for others. Management does not anticipate material losses on any deficiencies.

EXCEL CO-OP, INC.
NOTES TO FINANCIAL STATEMENTS
August 31, 2006 and 2005

NOTE 5 - PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

	<u>2006</u>	<u>2005</u>
Land and land improvements	\$ 1,438,354	\$ 1,418,156
Buildings	4,778,957	4,498,305
Machinery and equipment	6,882,516	6,437,112
Delivery equipment	5,124,454	5,105,245
Work in process	<u>1,742,138</u>	<u>253,869</u>
	19,966,419	17,712,687
Accumulated depreciation	<u>12,026,139</u>	<u>11,836,199</u>
	<u>\$ 7,940,280</u>	<u>\$ 5,876,488</u>

NOTE 6 - INVESTMENTS

Investments consist of the following:

	<u>2006</u>	<u>2005</u>
Land O'Lakes, Inc.	\$ 1,896,853	\$ 1,838,081
Countrymark Cooperative, Inc.	1,288,151	1,115,896
CoBank, ACB	770,599	703,036
Cenex Harvest Sates	328,243	210,238
Agri Insurance Exchange	192,967	179,748
Top Sow , L.L.C.	20,310	20,310
Other	<u>159,471</u>	<u>136,439</u>
	<u>\$ 4,656,594</u>	<u>\$ 4,203,748</u>

Land O'Lakes, Inc., CoBank, ACB and Countrymark Cooperative, Inc. each hold a lien on their equities for any indebtedness the Cooperative owes to these cooperatives.

EXCEL CO-OP, INC.
NOTES TO FINANCIAL STATEMENTS
August 31, 2006 and 2005

NOTE 7 - NOTES PAYABLE TO BANK

At August 2005, the Cooperative had a \$14,000,000 variable rate seasonal line of credit payable to CoBank, ACB which expired January 1, 2006. On May 4, 2006 the seasonal line was renewed increasing the maximum borrowings on the line to \$15,000,000 which expires January 1, 2007. Interest accrues at CoBank's weekly quoted variable rate (8.10% at August 31, 2006) on the outstanding borrowings.

The loan agreement underlying the note payable to bank and long-term debt agreement (see Note 8) contain various restrictive covenants relating to maintenance of minimum working capital and other items. At August 31, 2006, the Cooperative has complied with all requirements.

The note payable and long-term debt are secured by substantially all assets of the Cooperative.

NOTE 8 - LONG-TERM DEBT

Long-term debt consists of the following:

	<u>2006</u>	<u>2005</u>
Note payable to CoBank, ACB for Cooperatives, requiring annual principal payments of \$400,000 through 2016; interest floats at CoBank's weekly quoted variable rate plus .25% (8.35% at August 31, 2006)	\$ 3,714,300	\$ 2,114,300
Current maturities	<u>420,000</u>	<u>400,000</u>
	<u>\$ 3,294,300</u>	<u>\$ 1,714,300</u>

Principal payments on long-term debt are due over the next five years as follows:

2007	\$ 420,000
2008	420,000
2009	420,000
2010	420,000
2011	420,000

The long-term debt is subject to the same restrictive covenants and collateralization described in Note 7.

EXCEL CO-OP, INC.
NOTES TO FINANCIAL STATEMENTS
August 31, 2006 and 2005

NOTE 9 - CAPITAL STOCK

The shares of capital stock authorized, issued and outstanding, by individual class are as follows:

<u>Class</u>	<u>Par Value</u>	<u>Shares Authorized</u>		<u>Shares Issued</u>		<u>Shares Outstanding</u>	
		<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>
Preferred- non-voting	\$ 25	26,000	26,000	2,211	2,311	2,211	2,311
Common- voting	\$ 5	403,000	403,000	1,051	1,057	1,051	1,057

The preferred stock may be held by any person or entity and is preferential to common stock in the event of liquidation or dissolution. The preferred stock bears cumulative dividends annually at an annual rate of 6%. The Cooperative may redeem its outstanding capital stock at the discretion of the Board of Directors unless such approval is prohibited by law or by the financial condition of the Cooperative.

NOTE 10 - RETIREMENT PLANS

The Cooperative is a participant in a cash balance multiple employer pension plan. Plan assets are invested for the exclusive purpose of providing benefits to participants. Assets are invested primarily in equities to maximize the return on assets. Investments in additional asset classes with differing rates of return, volatility and correlation to other economic sectors are utilized to reduce risk and impact losses in single investments by providing diversification relative to equities. Securities will not be held in excess of the 10 percent limit imposed by ERISA.

EXCEL CO-OP, INC.
 NOTES TO FINANCIAL STATEMENTS
 August 31, 2006 and 2005

NOTE 10 - RETIREMENT PLANS (Continued)

Information regarding the Cooperative's defined benefit plan is shown below:

	<u>2006</u>	<u>2005</u>
Projected benefit obligation	\$ (5,801,269)	\$ (6,382,711)
Plan assets at market value	<u>4,229,520</u>	<u>3,759,265</u>
Funded status	\$ (1,571,749)	\$ (2,623,446)
Accumulated benefit obligation	(4,952,656)	(5,009,304)
Net Prepaid (accrued) pension cost recognized in the balance sheet	(706,897)	(724,814)
Additional minimum pension obligation recognized in the balance sheet	-	(481,167)
Benefit expense	229,135	215,360
Benefits paid	255,891	285,480
Employer contributions	330,597	175,828
Assumptions used:		
Discount rate	6.25 %	5.50 %
Expected return on plan assets	8.50 %	8.50 %
Rate of compensation increase	4.50 %	4.50 %

There are no participant contributions under this plan. Assets and obligations were determined three months prior to year-end.

The overall long-term rate of return on assets reflects the average rate of future earnings expected based on the target asset allocations and weighted market indexes measured over a market cycle of four to six years.

The Cooperative's pension plan weighted-average asset allocations at August 31, 2006 and 2005, base asset category are as follows:

	<u>2006</u>	<u>2005</u>
Equity securities	68.6 %	69.5 %
Debt securities	19.7	19.6
Real estate	6.1	5.5
Alternative	5.2	5.0
Other	0.4	0.4

The Cooperative expects to make contributions of \$333,699 to its pension plan in 2007.

EXCEL CO-OP, INC.
NOTES TO FINANCIAL STATEMENTS
August 31, 2006 and 2005

NOTE 10 - RETIREMENT PLANS (Continued)

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

2007	\$ 366,571
2008	311,287
2009	358,755
2010	380,286
2011	382,234
Years 2012 and thereafter	2,607,575

The Cooperative also has a retirement plan with 401(k) provisions which covers substantially all full-time employees. The Cooperative has agreed to match a percentage of employee contributions subject to limitations. The Cooperative's expense under this plan for the years ended August 31, 2006 and 2005 was \$114,236 and \$92,654.

NOTE 11 - LEASE COMMITMENTS

The Cooperative leases certain swine facilities and equipment under various operating leases expiring various dates through 2013. Under the terms of the swine agreements, the grower is responsible for the labor, utilities, taxes and maintenance related to the swine growing.

Minimum annual payments during the next five years are as follows:

2007	\$ 1,456,543
2008	1,368,202
2009	1,157,901
2010	1,019,360
2011	568,917
Thereafter	<u>483,334</u>
	<u>\$ 6,054,257</u>

Total rent expenses for the years 2006 and 2005 were \$1,722,829 and \$1,532,231, respectively.

EXCEL CO-OP, INC.
NOTES TO FINANCIAL STATEMENTS
August 31, 2006 and 2005

NOTE 12 - COMMITMENTS AND CONTINGENCY

The Cooperative entered into an agreement on November 11, 1998 to purchase 26,000 weaner pigs a year at a rate of 500 pigs per week through December 2008. The purchase price of the pigs vary upon current hog, corn and soybean meal prices. Based upon historical prices of these products, it is estimated that approximately \$832,000 will be expended each year for the purchase of the 26,000 weaner pigs. Under the terms of the agreement, the minimum annual cost of the 26,000 weaner pigs is \$416,000. Management does not anticipate material losses in the fulfillment of this agreement.

The Cooperative has issued an irrevocable standby letter of credit through CoBank, ACB in the amount of \$160,000 as collateral to support a contract swine growers bank borrowings. There were no amounts outstanding on the letters of credit at August 31, 2006. The letters of credit will be reduced to the following balances as follows:

2007	\$	80,000
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Should the Company be required to issue payments related to the letter of credit, it would have recourse against the applicable contract grower as security has been given by the grower. The Cooperative has not accrued any potential loss related to this arrangement.

NOTE 13 - RELATED PARTY

The Cooperative had the following transactions and account balances with officers and directors for the years ended August 31, 2006 and 2005:

	<u>2006</u>	<u>2005</u>
Accounts receivable (net of deposits)	\$ 165,901	\$ 261,350
Accounts payable	-	80,775
Sales to related parties	2,225,745	1,709,118
Purchases from related parties	1,087,772	1,065,491

SUPPLEMENTARY INFORMATION

EXCEL CO-OP, INC.
SCHEDULES OF OPERATING EXPENSES
Years ended August 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Fixed facility expenses		
Depreciation	\$ 1,084,194	\$ 1,061,518
Rent	331,666	158,766
Insurance	40,133	64,411
Property taxes	<u>51,608</u>	<u>90,742</u>
	1,507,601	1,375,437
Employee cost		
Wages and commissions	4,468,261	4,588,931
Payroll taxes	328,371	300,944
Pension expense	333,354	215,360
401(k) expense	114,236	92,654
Group insurance	303,253	265,186
Other insurance	40,063	90,125
Outside labor	17,617	27,506
Other employee cost	<u>57,107</u>	<u>50,520</u>
	5,662,262	5,631,226
Other operating expenses		
Repair and maintenance	460,359	418,272
Supplies and postage	187,797	209,585
Truck and mobile equipment	967,033	859,239
Power, water and fuel	392,501	324,670
Communications	98,311	99,292
Advertising	7,044	6,619
Promotions and meetings	132,454	102,435
Property tax	96,530	169,749
Insurance on inventory and other	343,030	402,749
Directors fees	74,703	52,048
Professional services	226,295	196,160
Travel	55,796	50,544
Bad debts	-	20,977
Miscellaneous other expenses	171,804	167,391
Gain on sale of property and equipment	<u>(195,486)</u>	<u>(58,144)</u>
	<u>3,018,171</u>	<u>3,021,586</u>
 Total operating expenses	 <u>\$ 10,188,034</u>	 <u>\$ 10,028,249</u>