Agricore United
(AU:TSX)

THE COMPANY

Agricore United was created via the merger of United Grain Growers Limited and Agricore Cooperative Limited, effective November 1, 2001. Based in Winnipeg, the Company supplies a wide range of agriculture-related goods and services to Western Canadian farmers. Agricore United is also responsible for handling, merchandising and marketing major types of grain both domestically and internationally. The Company strives to meet the complete needs of its customers through complementary business lines that include food-processing, agricultural publications and financial services.

FINANCIAL DATA

	1999	2000	2001
Earnings per Share ($)	0.15	0.06	0.91
Price to Earnings (times)	60.0	150.0	9.9
Dividend ($)	0.25	0.25	0.25
Dividend Yield (%)	2.78	2.78	2.78
Book Value ($)	12.56	12.14	12.62
Price to Book (times)	0.72	0.74	0.71

HISTORICAL SHARE PRICES

WHY ABC FUNDS BOUGHT AGRICORE

Agricore United, one of the largest "agri-businesses" in Canada, operates through four principal business segments. Crop Production Services, which accounts for approximately 53% of earnings, encompasses the sale of seed, fertilizer and crop protection products. Grain Handling and Merchandising, totaling 34% of earnings, involves the handling, transportation and merchandising of various types of grain. Agricore's Livestock Services segment, which contributes about 8% to earnings, manufactures and sells livestock feed and is expected to be the fastest growing component in the near future. The remaining balance of Agricore's earnings comes from the Complementary Business segment, which includes such diverse operations as food and oilseed processing, farming publications and niche financial services. Essentially, Agricore United is positioned to generate revenue and earnings at each stage of the crop production process and has diversified its operations in order to reduce earnings volatility.

The rationale behind the merger of United Grain Growers and Agricore Cooperative was to create a more competitive and profitable business, with greater liquidity for its shareholders. The combined entity is now a leading player in each of its business segments and is poised to build on this strong business platform. Market share is particularly important for Grain Handling and Merchandising since profitability is dependent on throughput volume, which lowers the average cost per tonne. The other segments will benefit from the geographically diversified retail distribution outlets, grain elevators and port terminals across the three Prairie Provinces as well as British Columbia and Ontario. After a four-year expenditure program, the strategic focus has shifted to the integration of the two companies, the elimination of redundant systems and the amalgamation of the distribution and transportation networks. Management expects to achieve cost savings or synergies from the merger of almost $47 million on an annualized basis.

In conjunction with the merger, Agricore United took the opportunity to complete an offering of 13 million shares and raised some capital in December 2001. The proceeds provided additional financial flexibility, which could be used for debt reduction or employed to acquire properties or complementary businesses. The recent trend in the grain handling industry has been toward "high-throughput-elevators" (HTEs) that are capable of loading 50 or more rail cars with grain within 12 hours. Agricore currently has 51 of such elevators and plans to consolidate and rationalize older, smaller and less efficient grain elevators. By transferring operations to these HTEs, Agricore will further reduce costs and improve profitability, thus building shareholders' equity.

Once the balance sheet effects of the merger and share issue are considered, Agricore United is currently trading at a discount of between 20% and 30% to its tangible book value and yields 2.8%. We expect this discount to narrow as Agricore's experienced management, led by Brian Hayward, demonstrates its ability to realize synergies and achieve operational efficiencies. Intriguingly, Agricore has an established strategic alliance with Archer Daniels Midland (ADM), one of the world's leading agri-business. ADM currently owns approximately 19% of Agricore United and could potentially increase its ownership stake at some point in the future. Despite the impact of a drought on the 2001/2002 crop-year, we believe that the Company has an enviable position within its industry. Without a doubt, farming is big business and Agricore United should be able to build solid shareholder value throughout the agricultural cycle.

ABC Funds
February 22, 2002

UPDATES

Agricore United has reported its first quarter of consolidated results after the merger of United Grain Growers and Agricore Cooperative. For the quarter ended January 31, 2002 Agricore reported a net loss of $11.8 million or ($0.29) per share. Unfortunately, this seasonally weak period was also adversely affected by last summer's drought, which reduced grain-handling volume and skewed fertilizer sales.

Although the earnings were soft due to unusual weather patterns, we believe that the real story was the progress made on the integration of the two entities. Recall that management's stated objectives are to achieve $12.2 million of synergies in fiscal 2002 and $24.7 million over the twelve-month period ended October 31, 2002. In total, $49 million of cost savings are expected by July 31, 2003, the first complete post-merger fiscal year. In the first quarter, operating expenses declined $12.5 million, excluding the impact of the rapidly growing Livestock segment. Consequently, we believe that management, led by Brian Hayward, is ahead of schedule on the integration and cost cutting initiatives.

Along with the financial results, two other interesting announcements have been recently released. First, Agricore United's country employees have voted for a direct working relationship instead of representation by a union. The outcome is not expected to have a noticeable impact on operations or financial performance. However, it was reassuring to see that the Company's employees were supportive of management. Second, Agricore has entered into a five-year agreement to securitize the Company's Canadian Wheat Board receivables. Management has estimated that this will reduce short-term borrowing by approximately $80 million over the course of the year, which will obviously reduce interest payments.

ABC Funds
May 31, 2002

Agricore United recently released financial results for its fiscal year ended July 31. These financials comprised nine months of consolidated operations and three months of UGG’s operations on a standalone basis. In the traditionally strong fourth quarter, Agricore United earned $39 million or $0.86 per share. For the full year, the Company reported earnings of $10 million or $0.25 per share. Excluding asset sales and unusual items the actual results were closer to breakeven. If we further adjust the numbers and assume that the merger was effective for the full 12-month period, Agricore United lost $6.5 million on a pro-forma basis.

These results must be put in the context of one of the most difficult operating environments that the Company has ever faced. On a year over year basis, the drought reduced Crop Production Services sales by 11% to $699 million. However, Agricore United was able to maintain its market share in this business segment. For the Company’s Grain Handling division, volumes declined by the same percentage as the industry, or approximately 36% for the quarter and 21% for the year, again implying that Agricore was able to protect its share of the market.

Digging deeper into the press release, it is apparent that the severity of the drought has obscured the tremendous cost reductions that management has achieved since the merger. The Company’s own estimates originally pegged cost savings at $50 million by July 31, 2003. However, management is significantly ahead of these projections and achieved synergies of $66 million as early as July 31, 2002. Forecasted cost reductions are now expected to total $80 million, a testament to management’s ability and determination amid an incredibly difficult operating environment.

In addition to the earnings announcement, several press releases have recently come across the newswire. On September 19, 2002 the Board of Directors cut the dividend from $0.25 to $0.075 per share in the interest of fiscal prudence. Although disappointing, Agricore is proud of its record of paying at least a nominal dividend in 92 of the past 95 years. Agricore’s financial flexibility was further enhanced with the sale of $100 million of 9.0% convertible unsecured debentures on November 11, 2002. If no attractive acquisitions become available, the proceeds will be used for general corporate purposes, including the reduction of bank indebtedness.

Although profitability has been disappointing due to the drought conditions in Western Canada, we continue to see long-term value in this Company. Management is working hard on those factors over which they can exert influence, such as market share and cost reduction. Once the weather normalizes, Agricore’s earnings power and cash flow generation ability will improve significantly. Under normalized conditions, every incremental tonne of grain that Agricore handles will create an additional $20 of gross profit. With low capex requirements going forward, cash flow will improve in a similarly impressive fashion.

ABC Funds
November 22, 2002

With the merger of United Grain Growers and Agricore Cooperative essentially complete, the outlook for the Company now depends almost entirely on the weather. Management has done all they can in terms of controlling costs, protecting market share and improving efficiency. We are currently monitoring such factors as snow pack conditions, precipitation relative to average levels and forecasted spring precipitation across the prairies. Normalized crop production and the associated spending are highly dependent on a return to historic growing conditions.

For the Company’s seasonally weak first quarter, Agricore United reported a loss of $0.45 compared to a loss of $0.29 last year. The bulk of this shortfall was due to the lagged effect of the 2002 drought, as grain handling volumes declined in tandem with the 44% industry-wide contraction. However, management believes that positive signs for the 2003 growing season are beginning to appear. Revenue from crop production services increased $13.1 million to $72 million from last year, an increase of 9%. Further, pre-paid sales orders, which are not booked until delivery and therefore did not impact the current quarter’s results, increased $35 million or 40% from last year. After two consecutive years of drought, higher soil moisture levels seem to have farmers looking for ways to maximize crop yield.

When will investors see any turnaround? With 75% of farm supplies sold in May and June, we may have to wait until the third quarter before we see a significant year over year improvement in the financial results. Further, it could be September or October before the 2003 harvest begins to have an impact on grain handling volumes. However, the stock market typically acts as a forward discounting mechanism and will look ahead for any signs of a recovery. One such optimistic sign was a recently released Agriculture and Agri-Food Canada report, “Agroclimate Outlook for the Prairies”, that indicated good potential for more normalized weather conditions in 2003. If soil moisture levels continue to improve and farmers follow-through with their planting intentions, Agricore United should demonstrate some serious earnings leverage to the recovery in the agricultural sector.

ABC Funds
April 4, 2003

For several quarters now, Agricore’s President Brian Haywood has said, “the recipe for success is to just add water”. After two years of drought, moisture levels have finally returned to more normalized conditions with decent precipitation last winter and spring. Statistics Canada has recently released figures for crop production in 2003, which predicted a significant improvement on a year over year basis. For example, total wheat production is forecasted to increase 36%, from 16.2 million tonnes in 2002 to 22.0 million tonnes in 2003, just below the five-year average of 22.9 million tonnes.

The Company’s financial results have already begun to turn on the back of higher crop input sales. In the third quarter of 2003, Agricore earned $0.96 per share compared to $0.86 the previous year. Management subsequently raised the annual dividend to $0.12 per share after reducing it to $0.075 more than a year ago. Although Agricore’s stock price has responded to the improving weather conditions, the Company still trades at a 30% discount to its book value of $10.96.

Once Agricore begins “firing on all cylinders”, with each division making a positive contribution to the bottom line, we expect the valuation discount to narrow. In the most recent quarter, the Crop Production Services Division generated most of the profit with farmers spending on seed, nutrients and crop protection products to maximize the quality and yield of their crops. This will lead to improved volumes at the Grain Handling Division toward the end of 2003 and into 2004. It is important to remember that the Company’s results are highly seasonal and we cannot extrapolate third quarter results for the balance of the year. Having said that, we look forward to a normal crop cycle so that we can finally see the positive impact of the merger synergies, the cost cutting program and the reduced leverage on the Company’s earnings power.

ABC Funds
October 17, 2003

We have sold our entire position in Agricore United. We believe that management, led by Brian Hayward, is doing an excellent job achieving synergies and realizing cost reductions after the merger of United Grain Growers Limited and Agricore Cooperative Limited. However, factors beyond management’s control have led to disappointing performance throughout 2002. A once in a century event of two back-to-back years of drought depressed the Company’s results. When soil moisture levels finally improved, Agricore’s stock recovered in anticipation of more normal grain handling volumes.

Unfortunately, the past winter seems to have been quite dry and although spring rains are forecasted to reach normal levels, we feel caution is warranted. Should the moisture levels improve, we have no doubt that the Company can generate a significant amount of cash. But we are just not willing to bet on the weather given other fundamentally attractive opportunities in the market.

ABC Funds
March 26, 2004