

Manufacturers' Steel Prices to Slowly Ease, But the Higher Price Floor is Here to Stay

John Anton, ferrous metals industry analyst, Global Insight Steel Service, provided two focused sessions outlining the steel situation and forecast at April's 2005 Farm Equipment Manufacturers Assn. meeting in Phoenix. If there was one central theme to his presentation, it was that each of the farm manufacturers in the room must understand the world dynamics governing steel supply, demand and, of course, the price for the material being delivered to their shops.

Global steel production exploded in 2002, going from 650 million metric tons in 1992 to 1.1 billion. Annual growth rates of 2.1% were seen from 1994 through 2001, followed by a growth rate of 9.2% from 2002 through July 2004.

The result was steel pricing that increased by 100-280% (depending on the product). In demonstrating the problem for farm equipment and other manufacturers, he noted that prior to the run-up in price, 45% of a fabrication's cost was in steel, 45% in labor and 10% in energy and overhead. "So, if steel costs double, the price of the fabrication should have risen by 20%," Anton says. "Fabricated metal prices only rose 9% however, so the difference came straight out of profits."

According to Anton, steel demand remains firm, but less upward momentum is forecast. "Much of the recovery already took place in 2004," he says. "China will remain the big driver."

While U.S. supply has loosened, the global supply remains tight, he says. While high production and imports replenished inventories, U.S. consumption caused less available steel elsewhere. Raw material additions, he says, are the key to relief.

Anton expects that prices will continue to ease. "High

Continued on page 2



Fig. 1. Global steel production was up 40% since January 1995, but raw materials expansion did not keep pace. "As long as there was a surplus, no one noticed," says John Anton. "But furnace capacity eventually hit a materials restraint, which is why prices exploded."

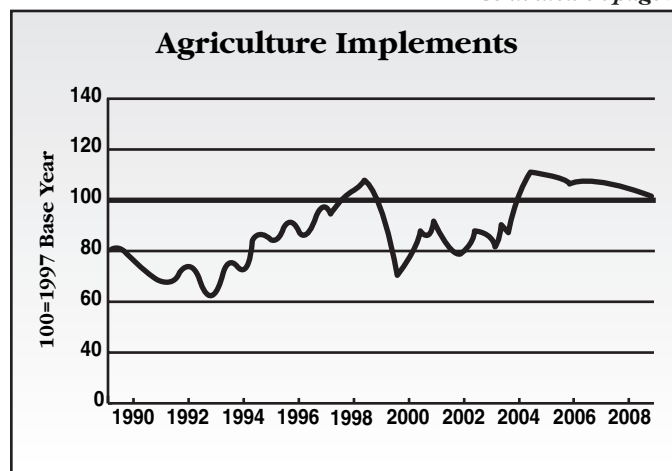


Fig. 2. This chart shows the demand curve for agricultural implements from 1990 through 2008. "Overall, it's a strong profile, showing some weakness in 2008," says Anton.

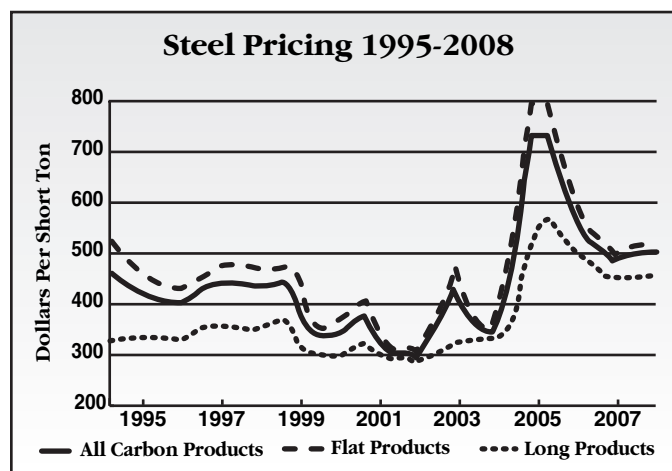


Fig. 3. This chart shows the "rapid-rise, slower descent" price activity for steel products.

GLOBAL INSIGHT'S STEEL FORECAST ASSUMPTIONS

1. U.S. demand grows slower in 2005 and plateaus in 2006.
2. China demand continues to grow strongly for the first half of 2005, but the breakneck pace will then moderate.
3. Western Europe and Japan are in danger of stagnating again; Central and Eastern Europe are looking strong.
4. Apparent supply in the U.S. was too strong and inventory tightness became inventory surplus.
5. High prices are spurring investment in raw materials, such that global supply will be much better with each passing quarter.
6. The dollar will continue declining until 2007, and will stay low. "This is very good when you're selling the finished product, but not so good when buying raw materials," he says.

input costs and the weak dollar will prevent a collapse, and more supply means lower prices." However, prices will not fall anywhere close to the rate at which they rose, and manufacturers can expect the new pricing floor to be higher than ever before, he says.

It's a Global Market

The steel market must be viewed globally, he says. U.S. apparent consumption now makes up only 13% of the world's total, and China (which accounted for 61% of the 40% global growth in steel production since 1995) is now three times larger in production and consumption than the U.S. The U.S. doesn't have enough capacity to fulfill its own needs and must import 20-30% of the tonnage it uses each year.

One cannot take his eyes off of the global market, for the following reason. "If China gets the iron ore, scrap and coke, then those materials are not available to the U.S. unless we outbid them," says Anton. "That is, unless prices go up."

"China's economy is growing at

STEEL'S GOOD NEWS/BAD NEWS FOR FARM EQUIPMENT MANUFACTURERS

GOOD NEWS	BAD NEWS
Prices are declining, and will continue to ease	Prices will be permanently higher than levels of 1998-2003
Supply is sufficient to meet demand	Capacity utilization is so high that any outage will be disruptive
The tumble in prime scrap costs undercuts surcharges	Raw materials remain tight, cost of making steel rises
End market demand will be strong in 2005	Demand outlook for 2006 is becoming worrisome

an unsustainable rate," says Anton. "It should slow in 2005 and 2006, but is still fast compared to the rest of the world." Even though Chinese per-capita consumption grew to one-half of the U.S. level in just 8 years, there's still room to grow.

Meanwhile, Anton points out that India is poised to follow China with extreme growth of its own (although its economy will be less manufacturing-driven). "They have a massive population, living in near poverty, are liberalizing governmental policies aiding expansion and are outsourcing," says Anton. "Together, China and India ensure strong global steel demand over the next decade."

The Home Front

For the U.S., the fundamentals have definitely shifted. Consolidation has meant fewer steel mills with more power, and Anton expects more consolidation to come.

The weaker dollar changes the trade landscape in finished steel. "Imports are a choice of last resort, and exports are now a viable market," he says. "The dependence on imports may be untenable in the future."

Discussing the sharply-rising raw material picture, Anton noted that metallurgical coke could not be obtained at any price early last year, and scrap is twice as expensive as in January 2003. While new ore and metallurgical coal mines are being dug,

he expects little relief until 2006-07. Because the scrap supply cannot be increased easily (dependent upon junking of steel products sold 10-15 years ago), the integrated steel producers are in better shape than the mini-mills.

Raw materials, particularly imported ore and coke, will continue to be more expensive, he says. Meanwhile, scrap exports have become more lucrative, and domestic steel-makers will have to outbid the Turks and Chinese for these raw materials.

Anton believes that steel demand in the U.S. will not resume peak levels again until 2008. Demand is rising from the 2003 trough, yet still below 2000. "Demand fell 14%, but had only risen 6.8% through the fourth quarter of 2004."

Price Outlook

"Prices fell slightly in the fourth quarter of 2004, and will continue to ease through 2005," says Anton. "There should be more significant declines in 2006 and 2007 as ore and coke become more plentiful, and an uptrend in the long-term as demand keeps rising."

Some of the downpressures that could affect price are imports, inventory restocking and global pricing that is lower than that in the U.S. Factors that could increase price are shipping expenses, the possibility of faster growth in China, the global supply of raw materials and the strength of the dollar, he says.

AWW

AG INDUSTRY WATCH is published monthly for the farm equipment industry by Lessiter Publications Inc., P.O. Box 624, Brookfield, WI 53008-0624. © 2005 by Lessiter Publications Inc. All rights reserved. Reproduction in any form of this newsletter content is strictly forbidden without the prior written consent of the publisher. Please send any address changes as soon as possible to the address shown above.

U.S., Canada and Mexico print subscriptions are \$349 per year. Save \$50 by receiving *Ag Industry Watch* each month via E-mail Internet access at only \$299 per year. International print subscriptions are \$449 per year. Send subscriptions to: *Ag Industry Watch*, P.O. Box 624, Brookfield, WI 53008-0624. Fax: 262/782-1252. Phone: 262/782-4480 or 800/645-8455 (U.S. only). E-mail: info@lesspub.com.

AGCO 1st Quarter Revenues Grow 34% in North America

With its May 3 first quarter announcement, AGCO's earnings appeared to fall in line with analysts' estimates. While revenues increased 34% in North America and 11% in Europe, these gains were offset by a 13% decline in South America.

Sales grew \$1.256 billion from \$1.115 billion, driven by growth in Western Europe and North America, as well as a 4% gain from currency translation. Net income at AGCO fell to \$21.5 million compared with \$25

million in the first quarter of 2004.

Company officials said operating margins fell as retail sales of tractors sank 16% from a year earlier. Retail sales of combines dropped 59%, with sharp declines in both Brazil and Argentina.

UBS' Bleustein notes that management chose production levels of 40% above retail sales in the first quarter, and that operating margins declined to 5.4% from 6.2%. "Management says that margins declined because of weakness

in South America and the impact of the Euro/Real denominated cost exports to North America, partially offset by strength in Europe."

Bleustein notes that AGCO officials indicated some optimism regarding the North American market in the second half of 2005, noting the strength in orders and dealer optimism regarding the market. Because of the South American situation, AGCO expects its adjusted net income in 2005 to be flat to 5% higher than 2004. *AJW*

Initial USDA Forecasts Look Bearish for Machinery Sales

RW Baird's Robert McCarthy says that the first look at the USDA's crop supply and demand estimates for 2005-06 paints a bearish outlook for crop prices. And although year-to-date sales of large tractors are currently running ahead of 2004 levels, equipment demand in the near term may suffer from the absence of accelerated tax depreciation incentives and lower crop prices, he says.

"The USDA's first look at crop supply/demand estimates appears relatively unfavorable from a farmer cash flow perspective, and by extension equipment demand," he says. Below is a summary of the most recent report. **Corn** — Domestic corn production is expected to reach 10.985 billion bushels, a 7% decline from last year's record level. The lower production reflects a combination of lower planted acreage and yield estimates. Despite the production decrease, corn

ending stocks are forecast to increase 15% year-to-year as supply outpaces demand, reducing prices by 15%. Globally, the supply/demand picture should tighten marginally, with smaller crops expected in the U.S., Europe and Russia.

Soybeans — Domestic soybean production is projected at 2.895 billion bushels in 2005-06, an 8% decline from last year's record crop. Acreage and yield are expected to decline, likely due to reactions about Asian soybean

rust. Ending stocks are expected to fall, as dry weather in Brazil impacts expected yields and production and increases demand for U.S. exports.

Wheat — "Wheat's outlook appears to be the most bearish," says McCarthy. U.S. wheat production is forecast to increase 1% year-to-year with harvested acreage up 2%. Domestic wheat stocks are forecast to rise 25% year-to-year as exports decline 10% due to higher exportable supplies in Europe, Ukraine and Russia. *AJW*

	Corn		Wheat		Soybeans	
	2005-06	% Change	2005-06	% Change	2005-06	% Change
Area Planted	80.90	-0.6%	58.60	-1.8%	73.90	-1.7%
Yield	148.00	-7.7%	42.70	-1.2%	39.90	-6.1%
Production	10985.00	-7.0%	2185.00	1.3%	2895.00	-7.8%
Exports	1950.00	8.3%	950.00	-9.5%	1125.00	2.3%
Total Use	10670.00	1.0%	2118.00	-5.2%	2964.00	2.1%
Ending Stocks	2540.00	14.7%	678.00	25.3%	290.00	-18.3%
Average Farm Prices	1.75	-14.6%	2.80	-17.4%	5.20	-8.0%

FARM MACHINERY TICKER (AS OF 5/12/2005)

Mfr.	Symbol	5/12/05 Price	4/13/05 Price	1-Year High	1-Year Low	P/E Ratio	Avg. Volume	Market Cap.
AGCO	AG	\$17.79	\$17.27	\$23.13	\$16.50	10.53	1.12 M	1.61 B
Alamo	ALG	\$19.24	\$23.91	\$29.23	\$14.40	13.84	18,900	187.47 M
Art's Way	ARTW	\$5.92	\$7.87	\$11.50	\$3.98	6.73	108,100	11.47 M
Caterpillar	CAT	\$88.88	\$88.60	\$99.96	\$68.50	14.36	2.97 M	30.37 B
CNH	CNH	\$17.16	\$18.26	\$21.08	\$16.18	19.50	76,000	2.30 B
Deere	DE	\$60.51	\$64.62	\$74.93	\$56.72	10.49	1.88 M	14.92 B
Gehl	GEHL	\$28.70	\$25.24	\$30.83	\$14.85	13.05	31,800	190.71 M
Kubota	KUB	\$26.30	\$26.45	\$28.46	\$19.05	64.15	5,600	7.05 B

Will Government Aid Help Equipment Sales in Canada?

Following last month's announcement of the Canadian government's \$1 billion aid package to boost the farm economy, *Ag Industry Watch* asked John Schmeiser, executive vice president, Canada West Equipment Dealers Assn., for his take on how farm equipment sales might be impacted.

While he says that Canadian farmers appreciate the aid received from both the federal and provincial governments, it was not the announcement that the industry was looking for. "Financial assistance has always been received as a short-term solution — the real need is for the border to

open," he says. "Our farmers and agricultural community have always believed that the delay in opening the border was related more to politics than science.

"We were ready to believe that the border would open on March 7. It was the further delay because of the Montana court's decision on the R-Calf lawsuit that prompted our federal government to announce a new aid package. It will make a difference though, to the producer, dealer and manufacturer."

When asked if it would spur some equipment sales, Schmeiser responded,

"Probably not, as it will just serve as another stop-gap measure. Equipment sales in under 100 hp tractors and hay tools continue to be depressed. No one is predicting a glut of new sales because of the government assistance."

Schmeiser says many are calling for the federal government to provide assistance for new processing facilities. "This will lessen our dependency in the U.S. market (which would hurt the U.S. in the long run), and assist us in marketing processed beef in world markets. The feds are looking at this, but no announcements have been made yet."

AWW

Gehl Reports Record Quarterly Sales, Raises Yearly Outlook

Gehl Co. reported record quarterly net sales of \$119 million for the first quarter, an increase of \$34.3 million (41%) from the first-quarter of 2004. The bulk of the growth was in construction equipment sales (up 54%), but the ag equipment side also saw a 16% increase vs. the first quarter of 2004.

While the ag growth looks modest compared to the construction equipment picture, Baird's Robert McCarthy says, "We understand that the year-to-year sales growth of material handling equipment sold through Gehl's ag dealers likely approximated the surge of the construction equipment segment." He estimates that ag equip-

ment sales increased 34% over the fourth quarter of 2004.

Gehl is raising its sales outlook for the year, with 2005 net sales in the range of \$440-\$460 million. "Our first quarter results and our current backlog exceeded our initial forecast and confirm the strength of the market," says William Gehl, chairman/CEO. "We anticipate the additional sales growth and our cost-control efforts to drive increased earnings for the remainder of the year."

McCarthy notes that easing production constraints will facilitate top-line growth in the near term, while Gehl's plant expansion will accommodate 2006 growth. "Future sales growth

will benefit from the increased manufacturing capacity at Gehl's Yankton, S.D., facility," he says. The new production space will be used to manufacture telescopic handlers, increasing production capacity by 50% for one of Gehl's best-selling lines.

AWW

GEHL 1ST QUARTER RESULTS

(000s OF DOLLARS)

	1st Qtr 05	1st Qtr 04
Net Sales	\$119,041	\$84,687
CGS	\$95,500	\$67,291
Gross Profit	\$23,541	\$17,396
Net Income	\$4,924	\$2,905

Farm Equipment Industry Newsmakers

Kverneland president & CEO, **Frode Berg**, referenced in last issue's "Norway's Kverneland Group Addressing Growing Pains" (p. 6), has resigned to take up "a leading position in another company."

John Deere has signed an agreement with Pakistan's **Agro Tractors** for a new Rs-600 million factory that will produce 15,000 tractors per year. Representing Deere's first manufacturing facility in the country, the joint venture is also expected to produce combines as demand grows.

Feterl Manufacturing Corp., Salem, S.D., announced on May 4 that it purchased the manufacturing rights for all models of PUG CATVs and the Dig-It compact towable backhoes. Both lines will be produced in Salem. Production of the CATVs will begin this August, with the Dig-It line in production by Spring 2006.

AGCO announced on April 22 that Valtra engineering, administration and marketing will be consolidated in Suolahti, Finland, where a new engineering center will also

be built. These business units were previously in Jyväskylä and Helsinki, Finland. Construction on the new center begins immediately, with all operations relocated by August 2006.

Anjanikumar Choudhari is the new President, Farm Equipment Sector, of India's **Mahindra & Mahindra Ltd.** He replaces **K.J. Davasia** who retired in January 2005 after more than four decades with the company. Choudhari was also appointed chairman of Mahindra USA Inc., the wholly owned subsidiary based in Tomball, Texas.

The credit, insurance and financial service offerings of **Case Credit** and **New Holland Credit** brands have been combined and re-branded as "**CNH Capital**" in the U.S. and Canada. The company's financial services business in Europe, Latin American and Australia already operate as CNH Capital, one of the largest equipment finance organizations in the world with a total managed portfolio of more than \$13 billion. The unit contributed a record \$159 million in net income to CNH Global in 2004.

CNH Nets \$15 Million in 1st Quarter, Addressing Capacity Issues

In late April, CNH Global reported first quarter 2005 net income of \$15 million, compared to a first-quarter 2004 net loss of \$9 million. Ag equipment net sales were \$1.9 billion for the first quarter, very much in line with last year. Total unit sales of CNH tractors and combines fell by 5% compared to the first quarter of last year. "We attribute the company's underperformance to limited manufacturing capacity in North America and increased competition from Landini and Claas in Europe," says Andrew Obin, Merrill Lynch.

First quarter 2005 production of tractors and combines was about 45% higher than retail, following the company's normal pattern to increase company and dealer inventories in anticipation of the spring selling season. Ag equipment gross margin declined compared to the prior year's first quarter, primarily due to lower volumes of high-margin combines.

"In total, worldwide industry retail unit sales of agricultural tractors and combines continued at last year's high levels in the first quarter," says Harold Boyanovsky, CNH president and CEO. "In this strong industry environment, our net price realization efforts successfully enabled us to offset significant economic and materials cost increases in the quarter — increases which were in excess of economic forecasts. In addition, our industrial efficiencies offset other cost increases."

For the full year 2005, CNH expects the ag and construction equipment markets to remain strong, "especially in North America for agricultural equipment."

Obin notes that CNH's "top-line growth was slightly better than expected, but its operating margin fell short due to continuing weakness in the ag equipment division operations." He says that the declining ag equipment volumes reflected the significant slowdown in South American and lower manufacturing capacity for combines in North America, due to the

shutdown of the East Moline facility a year ago. "CNH is consolidating its combine facility in Grand Island, Neb., and the company expects its 2005 second-half combine production to be running at a higher level than in the same period a year ago."

UBS' David Bleustein points out that CNH management continues to forecast roughly flat full-year worldwide ag equipment markets. CNH forecasts industry unit sales in North American tractors up 5% (unchanged for 2005) and combines up 10% (vs. negative 5-10% growth). Western Europe tractors and combines are both flat (unchanged). The Latin American picture is expected to worsen for both tractors (-20% vs. losses of 10-15% earlier) and combines (-55% vs. -30% earlier.)

"Reversing recent market share losses, particularly in Europe, is a key priority for CNH's new management," says

Obin. "In the North American market, increased product availability in the second half of the year should go a long way toward reversing CNH's market share loss." He adds that it will be harder for the company to regain market share in Europe, where more competitors are willing to gain share through aggressive pricing. *AIW*

TABLE 1. CNH OPERATING PERFORMANCE FIRST QUARTER '04 VS. '05

	'04	'05	Change
Revenue			
Ag Equipment	\$1,919	\$1,931	+0.6%
Cons. Equipment	744	892	+19.0%
TOTAL	2,663	2,823	+6%
Operating Profit			
Ag Equipment	\$110	\$74	-32.7%
Cons. Equipment	7	25	+257.1%
TOTAL	117	99	-15.4%
Operating Profit Margin			
Ag Equipment	5.7%	3.8%	-190bps
Cons. Equipment	0.9%	2.8%	+190bps
TOTAL	4.4%	3.5%	-90bps

TABLE 2. CNH WORLDWIDE RETAIL SALES ESTIMATES*

	Worldwide '05	North America '05	Western Europe '05	Latin America '05	Rest of World '05
First Quarter 2005 Industry Unit Sales Estimate Compared with First Quarter 2004 Actual					
Agricultural Equipment:					
Agricultural Tractors:					
- Under 40 hp	n/a	-2%	n/a	n/a	n/a
- Over 40 hp	n/a	+14%	n/a	n/a	n/a
Total Tractors	+1%	+6%	-2%	-4%	0%
Combine Harvesters	-20%	+39%	-6%	-52%	24%
Total Tractors and Combines	0%	+6%	-2%	-16%	+1%
Construction Equipment:					
Light Construction Equipment:					
Tractor Loaders & Backhoes	+21%	+20%	+2%	+63%	+27%
Skid Steer Loaders	+5%	+4%	+20%	-6%	+1%
Other Light Equipment	+17%	+47%	+14%	-10%	7%
Total Light Equipment	+14%	+17%	+14%	+37%	10%
Total Heavy Equipment	-5%	+19%	+16%	+26%	-26%
Total Light & Heavy Equipment	+6%	+18%	+14%	+31%	-11%
Second Quarter 2005 Industry Unit Sales Forecast Compared with Second Quarter 2004 Actual					
Total Tractors	-4%	+4%	-8%	-21%	-7%
Combine Harvesters	-19%	+3%	+8%	-63%	-24%
Total Light Equipment	+8%	+8%	+9%	+28%	+3%
Total Heavy Equipment	+3%	+10%	+5%	+10%	-4%
Full Year 2005 Industry Unit Sales Forecast Compared with Full Year 2004 Estimated Actual					
Total Tractors	-2%	+4%	-5%	-19%	-4%
Combine Harvesters	-18%	+9%	+1%	-54%	-14%
Total Light Equipment	+8%	+10%	+6%	+12%	+7%
Total Heavy Equipment	+3%	+6%	+5%	+2%	0%

* Excluding India

Farm Equipment Retail Sales Dip in April, But 2005 Still Pacing '04

After disappointing farm equipment retail sales in March, total North American unit sales again fell 6.1% vs. a year ago in April, the key month for sales in the spring selling season. Nevertheless, total North American unit sales were still 1.5% ahead for the first four months of the year vs. one year ago. April's figures are found on p. 7.

While April 2005 failed to keep pace with April 2004 in all but two U.S. sales categories (40-100 hp tractors and total 4WD tractors), the story was different on the Canadian side. Only 100 hp tractors failed to match last April's figures, and Canadian unit sales as a whole were 12.6% above last April's levels.

In the U.S., the greatest activity last month was in combines and 100 hp tractors, which both increased 47% over March. In Canada, dramatic increases occurred in all categories in April, with increases ranging on the low end from 95% (combines) to 121% (under 40 hp tractors).

A summary of the U.S. activity by

class is as follows:

Utility Tractors — Increased 4.1% in April, following a 25.3% increase in April 2004.

Row-Crop Tractors — Fell 3.7%, following a 47.5% increase in 2004. UBS' calculations predict a seasonally adjusted rate of 22,000 units, up from the 20,200 units seen in the prior 12 months.

4WD Tractors — Increased 22.5% in April, following a 15.5% increase in April 2004.

Combines — Fell 1.1% in April, following the same percentage loss in April 2004.

Inventories of utility tractors, row-crop tractors and 4WD tractors remain above last year's levels, while small tractors and combines are below last year's levels. "U.S. dealer inventories of large tractors rose sequentially on a days-sales basis in March," says Baird's Robert McCarthy. "OEMs appear to have appropriately gauged April demand."

"The April sales data reflects limited product availability from CNH

and Deere's unwillingness to give up its pricing power to gain additional volume as well as multiple hikes over the last 12 months," adds Andrew Obin, Merrill Lynch.

"We continue to expect 0-5% growth in U.S. farm machinery sales in 2005, as generally lower farm commodity prices are more than offset by strong livestock profitability, strong farmer balance sheets, low interest rates, a countercyclical farm program and multiple years of weak demand," says UBS' David Bleustein.

Year-to-date 2005 vs. 2004, combine sales (+23.4%) and 40-100 hp tractors (+13.4%) top the North American equipment list, which is pacing 1.5% ahead of last year. Sales of under-40 hp tractors (-6.6%) are the only North American category (and only U.S. category) year-to-date that cannot match last year's January to April sales figures. Canada has exceeded year-to-date sales in all categories with the exception of 4WD tractors (-13.2%). AWW

Farmers to Feel the Sting From High Fuel, Fertilizer Costs

With a barrel of crude oil now selling for as much as \$55 (vs. \$35 a year ago), all Americans are feeling the pinch every time they hit the fuel pumps. But farmers face a full frontal attack. They are being squeezed by higher prices for the diesel fuel that runs their tillage, seeding, harvesting and irrigation equipment, for the fertilizer made by

combining nitrogen with the hydrogen in natural gas and the cost to transport their crops. Farmers have seen the price of their fuel grow two-fold, from \$0.96 per gal. in April 2002 to \$1.97 in April 2005. Terry Francel, senior economist with the American Farm Bureau Federation, says U.S. farmers will spend 10% more this year — amounting to \$3

billion — on costs that include fuel and fertilizer. That \$3 million comes directly out of their income.

Because fertilizer manufacturers face higher natural gas prices, the prices that they charge have risen accordingly. Anhydrous ammonia now sells for \$416/ton, up from \$250/ton three years ago. AWW

Buhler Results Show that Price Increases Sticking

Buhler announced in late April that second-quarter earnings were up 4.2% to \$4.1 million compared to \$3.9 million for the same period a year ago. Revenues, meanwhile, were up 2.2% to \$64 million from \$62.6 million a year earlier.

Despite the second-quarter increase in net earnings, however, profits for the first half of the year fell to \$5.7 million from \$6.0 million in the first half of fiscal 2004.

Nevertheless, first-half revenues fared better, growing by 4.6% to \$109.8

million from \$104.9 million in the first 6 months of the previous year.

Ben Cherniavsky, Raymond James Equity Research, noted that the firm had notched its second consecutive quarter of sequential margin improvement. "This is an early indication, in our view, that the price increases implemented in early January are sticking, and in turn, providing a welcome relief from higher input costs, many of which are steel-related." He adds that management had continued to demonstrate good cost

controls, which were reduced by \$400,000 vs. a year ago.

As for the future, Buhler's Craig Engel says that "due to the uncertain, long-term reaction of our customers to our increased 2005 prices, we continue to forecast flat or slightly improved annual revenues, in spite of the increases we experienced during the first two quarters of the year." Cherniavsky believes fiscal year revenue will now total \$215 million, or \$5 million less than previously anticipated. AWW

Same Deutz-Fahr Acquires Croatian Combine Builder Duro Dakovic

Italian tractor and harvest machinery manufacturer Same Deutz-Fahr (SDF) has secured a low-cost manufacturing facility — and a bridgehead into Eastern Europe — by acquiring a majority holding in Duro Dakovic psu of Croatia.

The business is being purchased from Duro Dakovic Holding, of which the Croatian government is a major shareholder, following a tender made under the state's privatization program. SDF will initially hold 86.4% of the shares and plans to secure outright ownership through an offer to small shareholders.

The total investment will amount to Euro 25m (\$32m), says SDF's CEO Massimo Bordi, who expects to break-even by the end of 2007 with sales of 1,000 combines annually, worth Euro 100m (\$128.4m), within 5 years.

Duro Dakovic psu, which will be renamed Same Deutz-Fahr Croatia, has produced Deutz-Fahr combines under license for more than 20 years. Current production will integrate with the bigger capacity "TopLiner" models to be built in Croatia.

These were previously made under contract at AGCO's Dronningborg Works in Denmark, which was scaled down to cut losses, and before that in SDF's own Lauingen plant in southern Germany. The group also has a marketing and manufacturing agreement for small- to mid-size combines with Sampo-Rosenlew of Finland.

"With this acquisition, we will continue to produce high-quality harvesting machines at competitive prices," adds Bordi. "Furthermore, it will serve as a technical and commercial support base for commercial expansion throughout the south Eastern Europe region."

SDF has reported a 11% increase sales revenues to Euro 905m (\$1.16bn) for 2004 while net profits more than doubled from Euro 10m to Euro 22m (\$12.8m to \$28.2m). The group sold 32,300 tractors, its best performance in the past 20 years.

AIW

APRIL U.S. UNIT RETAIL SALES



Equipment	April 2005	April 2004	Percent Change	YTD 2005	YTD 2004	Percent Change	March 2005 Field Inventory
Farm Wheel Tractors-2WD							
Under 40 HP	14,911	17,410	-14.4	36,394	38,961	-6.6	67,626
40-100 HP	7,856	7,549	+4.1	22,277	19,526	+14.1	31,874
100 HP Plus	2,783	2,890	-3.7	7,991	7,779	+2.7	6,383
Total-2WD	25,550	27,849	-8.3	66,662	66,266	+0.6	105,883
Total-4WD	658	537	+22.5	1,419	1,303	+8.9	1,211
Total Tractors	26,208	28,386	-7.7	68,081	67,569	+0.8	107,094
SP Combines	461	466	-1.1	1,378	1,113	+23.8	1,380

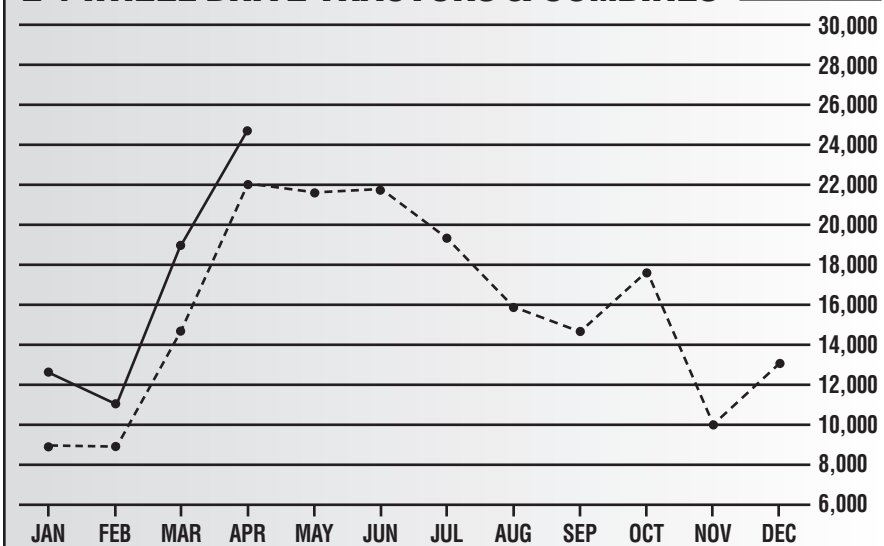
APRIL CANADIAN UNIT RETAIL SALES



Equipment	April 2005	April 2004	Percent Change	YTD 2005	YTD 2004	Percent Change	March 2005 Field Inventory
Farm Wheel Tractors-2WD							
Under 40 HP	883	688	+28.3	1,711	1,525	+12.2	4,356
40-100 HP	786	677	+16.1	1,738	1,637	+6.2	2,909
100 HP Plus	527	579	-9.0	1,103	1,074	+2.7	1,622
Total-2WD	2,196	1,944	+13.0	4,552	4,236	+7.5	8,887
Total-4WD	180	167	+7.8	269	310	-13.2	271
Total Tractors	2,376	2,111	+12.6	4,821	4,546	+6.0	9,158
SP Combines	117	102	+14.7	282	232	+21.6	460

U.S. UNIT RETAIL SALES OF 2-4 WHEEL DRIVE TRACTORS & COMBINES

— 2005
--- 5 year average



—Assn. of Equipment Manufacturers

Aptly Named Challenger Program Making Waves, Expects \$3-5 Million Profit This Year

According to Langenberg & Co.'s Charles Rentschler, the 15-year-old AGCO has a commanding lead in South America (the world's most rapidly growing market for ag equipment) and a respectable 20% share in Europe, but only a small, single-digit slice of North America.

The Challenger program was instituted by chairman and founder Bob Ratliff to change this picture, he says. Bought from Caterpillar for \$25 million in 2002, Challenger is an agreement whereby AGCO builds and sells the line of private-banded farm machines through Caterpillar dealers.

The significance of Challenger to AGCO is apparent in understanding that the U.S. market is \$10 billion per year vs. AGCO's worldwide revenues of \$5.4 billion. Since Challenger had U.S. sales of about \$300 million last year, achieving market share of 20% could add \$1.7 billion or 30% to AGCO's top line.

After visiting Caterpillar farm machinery dealers in Indiana and Ohio, Rentschler shared his observations on Challenger with *Ag Industry Watch*.

Minuses — While a significant portion of Cat's domestic dealers have set up truly independent ag machinery divisions, Challenger

competes for the attention of Cat's sales people, who are also selling farmers Cat-built products and combines from Claas. Some sense a contradiction within management between pushing the Challenger line while also promoting legacy brands such as AGCO, Massey-Ferguson and Fendt.

"Clearly, Challenger has product voids and insufficient domestic manufacturing capacity," says Rentschler.

Pluses — Rentschler believes that Cat's dealer network is the "greatest industrial-product distribution system

"There is a possibility of Caterpillar buying AGCO..."

in the world." With Cat's near-50% share of the construction market, farm machinery gives most dealers a nice diversification opportunity in similar equipment.

"Substantial numbers of Cat dealers worldwide are embracing the Challenger program, devoting dedicated facilities, working capital and personnel," he adds.

Rentschler also says that Cat's ag business model (aimed at the large, corporate-type farmer) is the way of the future, with minimal "brick-and-mortar" but large fleets of well-equipped and mobile-dispatched mechanics.

"By giving its dealers protected territories, Cat ensures distributors do not compete against each other, which is the opposite of Deere," he says. "The biggest competition for Deere dealers is themselves."

In early May, management reported that global Challenger sales grew 50% above the first quarter of 2004, with breakeven profitability. AGCO now expects a 25% increase for the full year, with an operating profit of \$3-\$5 million, coming off the \$3 million loss last year.

Noting that this loss has dimmed the viewpoint of many industry observers, Rentschler stresses that the Challenger program "has made incredible progress in a short period of time." In fact, he says that it is imaginable that Deere could be "toppled from the perch it has sat on for nearly 50 years as the nation's number-one farm machinery maker."

And, he adds, there is a possibility of Caterpillar buying AGCO. *AIW*

Subscribe Today To *Ag Industry Watch*!

Receive the best news coverage and analysis of the agricultural equipment industry each month.

Fill out and mail or fax your subscription today to 262/782-1252.

☐ Please start a 1-year print subscription for U.S., Canada or Mexico for \$349.

☐ Please start a 1-year E-mail subscription (12 issues) for \$299.

☐ Please enter my 1-year International subscription (12 issues) for \$449.

Name: _____

Address: _____ City: _____

State/Province: _____ Zip/Postal Code: _____ Country: _____

Phone: _____ Fax: _____

E-mail: _____

Enclosed is: ☐ Check for \$ _____

☐ MasterCard ☐ Visa ☐ American Express

Card #: _____ Expires: _____

Name on Card: _____

Signature: _____

MAIL TO:

Ag Industry Watch

P.O. Box 624

Brookfield, WI 53008-0624

FOR FASTER CREDIT CARD SERVICE:

Call: 800/645-8455 (U.S. only)

262/782-4480

Fax: 262/782-1252

E-mail: info@lesspub.com

PRIORITY CODE: AIW055