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# FARM EQUIPMENT's Ag Industry Watch

*News, Information & Analysis for the Ag Equipment Marketer* — *March 15, 2006*

## With New Product Launches, Challenger Now Considered a 'Real Player'

With its rollout of three major additions to its product line, including the industry's largest 4WD articulated tractor, at the National Farm Machinery Show in February, Challenger is positioning itself to take on the "big boys" in the ag equipment industry.

"The new AGCO-Challenger line of equipment is impressive," says Rich Keller, a Southern Indiana dealer that handles a competing line. "With the introduction of the new articulated tractor and the combine, these will make them a real player in the market."

In addition to their new MT900B series of wheeled-articulated tractors, with horsepower ranging from 430-570, AGCO also introduced its new Class VIII combine that features a 425-hp Caterpillar Engine featuring "the largest rotor in the industry."

The company also unveiled its lineup of 45-75 PTO hp utility tractors.

With these holes in its product line now filled, industry observers feel that Challenger has put itself in a position to compete with the other major tractor makers.

But questions remain about the perceived weakness in the Challenger distribution network. With a relatively small number of Cat dealers throughout the U.S., points of contact with the agricultural community is a concern in terms of convenience and service.

Challenger is the 4-year old arrangement between AGCO and Caterpillar in which AGCO provides a full line of private-branded products — from tractors to combines, to hay tools and other implements — for sale through Cat construction equipment dealers who want to diversify into the ag market. The partnership between AGCO and Cat calls for the Challenger brand to be sold only by Cat dealers.

According to Doug Griffin, director of Challenger sales and marketing for North America, "There are currently 41 contracted Cat dealers for Challenger. Those 41 dealers cover 93-94% of the agricultural opportunity in the country. We're not done with distribution. Strategic areas need new dealers. We're putting them in farm-friendly locations."

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## Dealers Say New and Used Equipment Inventories are Growing

Ag equipment dealers say that new and used equipment inventories have increased since the last UBS Investment Research's Semiannual Agricultural Dealer Survey in April/May 2005. Of the roughly 550 dealer responses to this question, 29% responded that inventories were either "Much lower than normal" or "Lower than normal" vs. 31% who responded either "Much higher than normal" or "Higher than normal." The remaining 39% responded "Normal."

**TABLE 1: DEALERS' VIEWS ON NEW EQUIPMENT INVENTORIES**

| Company | Much Lower Than Normal | Lower Than Normal | Normal | Higher Than Normal | Much Higher Than Normal |
|---|---|---|---|---|---|
| AGCO | 5% | 14% | 39% | 40% | 2% |
| Case-IH | 2% | 27% | 36% | 32% | 3% |
| Deere & Co. | 5% | 39% | 45% | 11% | 0% |
| New Holland | 2% | 23% | 38% | 36% | 1% |
| **Total** | **3%** | **26%** | **39%** | **30%** | **1%** |

In total, the results indicate that inventories increased slightly since the previous survey in which new inventory levels were below-normal. Based on current survey results, dealers believe new equipment inventories are now at roughly normal levels.

Of the dealer responses to the question on used equipment inventories, 35% responded either "Much lower than normal" or "Lower than normal" vs. only 24% who responded either "Higher than normal" or "Much higher than nor-

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**EXCLUSIVE BONUS REPORT IN THIS ISSUE**

**"The Agricultural Equipment Industry in Europe"**

*With New Product Launches, Challenger...Continued from page 1*

**A Problem-Solving Model.** In an interview with *Ag Industry Watch,* Randy Hoffmann, senior VP and GM of Challenger, says that the AGCO-Cat relationship will yield significant benefits over the longer term, and that Cat dealers bring a lot to the table. "The Cat guys can go after government business because they know it. They are used to the big machine business. They're comfortable in it. Some are already doing a great job in hay and other applications.

"Look at North American distribution farm equipment as a whole," he says. "There are some very good dealers out there, but there's a lot of them. Some are good but they're very limited capital-wise.

"Capital requirements are a huge need these days, especially when you consider that dealers are taking on high-ticket trades. This will become even more important as we move forward. The number of ag dealers is dwindling because of the capital requirements needed to grow."

Hoffman explains that Cat dealers are very sophisticated in terms of technology and products, they offer round-the-clock service capabilities and are well capitalized. "A good distribution business should look just like this. We will exploit Cat dealers to get where we need to be in terms of share, scope and profitability."

According to Martin Richenhagen, AGCO president and CEO, "Other competitors, like Argo, simply have too many dealers. That's a problem that must be changed. We can grow our distribution without hurting existing dealers. We do it through a differentiated product, exclusive for Challenger.

"AGCO believes in the relationship with Cat and the Cat dealers. It is the finest distribution method you could think of," he says.

Richenhagen recalls that initially, a lot of Cat dealers considered ag a major investment. "Some said they'd try it for 2-3 years and then decide whether they'd go for it," he said.

"A lot of them are now convinced that it is a business that they want to be in. They're hiring, putting in new outlets, investing in people, advertising and boosting service. They're optimistic that [being part of Challenger] is a great solution [way to expand their business]," says Richenhagen.

"If you look at where we are globally (citing the lead position in 60hp-plus tractors in South America and the market share leader in most European markets and the technology leader) there are a lot of elements that will make us more successful in North America," says Richenhagen. "What has been missing is the strong dealer who needs to invest. We want to be a major player."

**Learning Ag.** Hoffman says that the learning curve for the Cat dealers has been systematic and he's pleased with their progress after 3 years.

"Their learning curve is at various stages, as Cat dealers didn't know the ag customer. It's been an education for them in terms of the product and understanding the buyers. It has taken more time but the approach was methodical. We're getting there and they're doing everything that we're asking of them, and they have been aggressiveness in getting things right."

**The Service-Centric Model.** The way service is handled by the Cat dealers for the Challenger line is also new to the ag industry. Charlie Rentschler, an industry analyst for Foresight Research Solutions, in an earlier report on AGCO, says "We perceive that the Cat dealer method of dispatching mechanics in trucks to fix machinery on the farm is working splendidly.

"This, of course, is a new model compared to what we believe is the broken-down system of Deere and CNH Global, in what we have called the 'many small stores' approach. It seems clear that Deere and CNH would like to follow Cat's example," says Rentschler.

**Results.** From all appearances, it looks as if the young Challenger brand is already making its mark in the farm machinery industry.

"Challenger sales grew 30% last year alone," says Bob Crain, AGCO's new vice president and general manager for North America, who joined the company after at 20-year stint with New Holland. Many industry observers said that bringing Crain on board was a solid strategic move on AGCO's part.

Crain adds that the filling out of the Challenger lineup with the smaller tractors introduced at the Louisville show was important to the future growth of the brand.

"A good portion of the compact and utility tractor market is applicable to construction and industrial applications," says Crain. "We already seen significant sales gains in the past 18 months from the Cat dealers."

**Branding Focus.** Richenhagen says that AGCO will continue full speed ahead with its multi-brand strategy, but will push specific lines only where they make sense. "When we started 2 years ago, we took 26 brands down to 13. In South America, we have two brands, Massey Ferguson and Valtra and one in Europe (Fendt). In North America, we have Challenger. We are very careful not to lose the customers who are loyal to certain brands. Along with Challenger, we are very different from our competition.

"We believe the multi-brand strategy is very good because people around the world are loyal to brands just as they are loyal to colors in the U.S. Massey Ferguson has been around 170 years, with 180,000 units worldwide. While some are more niche like Valtra, there's no reason to push them out. We'll leave them where they're strong and not compete with others." AIW

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*New and Used Equipment Inventories...Continued from page 1*

mal." The remaining 41% responded "Normal." In total, the results indicate that dealers believe used equipment inventories are continuing at below-normal levels.

For the question on new equipment inventories, the national average response was 5.00 (normal), compared to the national average score of 4.15 (lower than normal) from the last survey conducted in April/May 2005. The survey results indicate that dealers believe new equipment inventories have increased to normal levels. Deere dealer responses resulted in the lowest average response of 4.08, indicating that Deere dealers view their inventory levels as the tightest. Of the four majors, only Deere dealers views their inventories as below normal.

**TABLE 2: DEALERS' VIEWS ON USED EQUIPMENT INVENTORIES**

| Company | Much Lower Than Normal | Lower Than Normal | Normal | Higher Than Normal | Much Higher Than Normal |
|---|---|---|---|---|---|
| AGCO | 4% | 33% | 35% | 26% | 1% |
| Case-IH | 3% | 32% | 43% | 20% | 2% |
| Deere & Co. | 2% | 27% | 50% | 21% | 0% |
| New Holland | 3% | 34% | 36% | 25% | 2% |
| **Total** | **3%** | **32%** | **41%** | **23%** | **1%** |

## Delivery Leadtimes

Dealers report that delivery leadtimes remain long, although they indicate that this has improved since spring. On the question on leadtimes, 34% reported that delivery leadtimes had "Become longer" vs. 20% who reported "Become shorter." The remaining 47% reported that leadtimes "Remained the same."

In the previous survey, 72% of dealers reported longer leadtimes, with only 4% reporting shorter leadtimes, indicating that dealers believe leadtimes have improved considerably, compared to the spring.

Despite the improving trend in delivers, dealers commented that availability remains challenging. They also noted that leadtimes vary by manufacturer and product type. Comments included: "John Deere is very independent in its approach to the problem," "low horsepower leadtimes are excessive," "leadtime is longer than floor plan," "4 to 10 months for it — the competitors love it" and "we are ordering non-engine equipment a year out — engine engineering is up 4-6 months."

The difference in leadtimes among manufacturers remain problematic for dealers as well:

"Companies only want to build on 'sold' orders," "majors are pushing their overhead down on dealers — they don't want to keep much inventory on hand — we have to order product 3-6 months in advance to get product for selling season," "Kubota is hard to get product from — lots of delays," "New Holland is the worst," "JD and NH in particular have decided that if you want one of their units you will wait, on tractors especially. You better order it 9 months ahead for even a shot," "CNH continues to look for ways to increase sales but with little product availability, on-the-ground deals keep going to the other guys," "very unpredictable, orders cancelled without notice," "With the Midwest farm belt sales weakening, it has opened up some availability to us on certain farm equipment." AIW

**TABLE 3: DEALERS' VIEWS ON EQUIPMENT DELIVERY LEADTIMES**

| Company | Become Longer | Remained the Same | Become Shorter |
|---|---|---|---|
| AGCO | 35% | 47% | 18% |
| Case-IH | 35% | 47% | 18% |
| Deere & Co. | 29% | 44% | 27% |
| New Holland | 36% | 48% | 16% |
| **Total** | **34%** | **47%** | **20%** |

**FARM MACHINERY TICKER (AS OF 3/10/2006)**

| Mfr. | Symbol | 3/10/06 Price | 2/10/06 Price | 1-Year High | 1-Year Low | P/E Ratio | Avg. Volume | Market Cap. |
|---|---|---|---|---|---|---|---|---|
| **AGCO** | AG | $17.52 | $17.52 | $21.46 | $14.60 | 12.97 | 1.44M | 1.71 B |
| **Alamo** | ALG | $21.34 | $22.80 | $ 25.85 | $18.04 | 15.93 | 9,600 | 208.00 M |
| **Art's Way** | ARTW | $6.08 | $6.00 | $11.50 | $4.50 | 12.16 | 5,400 | 11.97 M |
| **Caterpillar** | CAT | $70.95 | $68.75 | $75.50 | $41.31 | 17.56 | 4.34 M | 47.60 B |
| **CNH** | CNH | $25.20 | $20.08 | $26.02 | $15.79 | 36.00 | 218,700 | 3.37 B |
| **Deere** | DE | $74.97 | $73.62 | $79.00 | $56.99 | 12.60 | 1.81 M | 17.59 B |
| **Gehl** | GEHL | $30.00 | $29.37 | $35.05 | $14.83 | 15.23 | 105,500 | 360.30 M |
| **Kubota** | KUB | $47.40 | $45.24 | $49.56 | $24.20 | 11.67 | 30,700 | 12.49 B |

## Are Multi-Stores Paving the Way for Company Stores?

Will the rapidly emerging trend toward multi-store ag dealers open the door once again to the major equipment manufacturers giving company stores another try? Charles Glass thinks it might.

Responding to an article that appeared in the February 15 *Ag Industry Watch* that cited Case IH's potential interest in company stores ("Case IH Dealers Hear Clear Message on Competitive Lines" p. 8), Glass, who is an active participant in the Farm Equipment Manufacturers Assn. and an industry historian, says, "I found the position that Case IH is taking with its dealers that carry competitive lines interesting because I predicted these sorts of actions from the majors a couple of years ago." (See "The Farm Equipment Revolution is Already Underway," Special Management Report from *Ag Industry Watch*, 2005.)

"This is apparently coming from John Deere's success in eliminating competitive products from their dealerships over the past few years. Because of their success, Case IH, New Holland and Kubota have little recourse but to try to follow their lead."

Glass recalls the IH-owned dealerships of the early 1970s. "They failed miserably," he says, "because of the very limited oversight that the company had on the daily operations of these stores. But the new company store concept will be radically different from the independent store concept."

Unlike the poor communications and other management shortcomings that doomed the earlier "company store" model, the more recent success of the independently owned multi-store organizations is demonstrating that the model is more viable today.

"Successful multi-store operations are demonstrating that a new model of operation can be planted in each new store location — a principle similar to that used by the successful box stores," he says.

With the advanced communication technologies available today to allow headquarters to review activities of each individual dealership on a "real-time" basis, the new business model is far more viable today than even 5 years ago, says Glass.

"Secure satellite links allow the instantaneous transfer of data from the store to corporate offices," he explains. "The effectiveness of the store manager is enhanced because he knows that his every action is being observed and critiqued."

Glass points out that the process is already underway as seen with some OEMs buying construction equipment dealerships and forming a large group of company-owned stores.

"John Deere, for one, has quietly taken control of several CE stores and operates them under the name of Nortrax," Glass points out.

Nortrax, owned and operated by Deere, currently has 48 locations with more than 1,000 employees in 13 states.

"The success of the current multi-store operators has shown the OEMs that they can in fact operate company-owned stores profitably now. This will continue to be a growing trend," says Glass. "Independent dealer-owners are going to be very rare in the very near future. The retail outlets will either be owned by a large multi-location dealer or by the OEMs themselves." AIW

## Russia to Fund Improvement in Domestic Farm Machinery Sector

According to a report in the *Moscow Times*, Russia's cabinet approved a blueprint on March 9 to develop the country's ailing agriculture machinery industry. According to Prime Minister Mikhail Fradkov, 40% of farm equipment manufacturers in Russia (which provide only 35-60% of the machinery Russia's farmers require) are running at a loss.

The plan calls for the government to spend $35.6 million on research and development through 2008 to revive the stagnating industry and to improve conditions for farm equipment leasing. The cabinet called for the use of petrodollars from the nation's infrastructure fund.

Details of the strategy, which aims to boost production of tractors by 18% by 2008 and grain harvesters by 33%, must be finalized by the government by May 1. Russia is increasingly focusing on the agricultural sector, which is slated to receive $1.3 billion from the federal budget — 65% more than in 2005. Reviving the farming industry is among President Vladimir Putin's "national project priorities," along with housing, health care and education.

Machinery builders must consolidate if the industry is to survive and withstand foreign competition, says Agriculture Minister Alexei Gordeyev, proposing that "manufacturers be rounded up into two or three holdings."

To entice the injection of expertise into the farm machinery industry and to encourage production of equipment that is not manufactured by domestic companies, foreign investors would be offered conditions similar to those offered to foreign carmakers last April. According to the plan, foreign manufacturers willing to assemble farm equipment in Russia would be required to gradually increase the proportion of domestically produced parts from 25% in the first stages to 50% within 3-4 years.

Svetlana Tsvetkova, deputy head of the Russian office of Germany's Claas, the only Russian-based foreign maker of harvesters, however, doubts that such a measure would work. "This is impossible. The quality of Russian-made parts leaves much to be desired," she said. In addition, big farms are increasingly likely to opt for Western equipment due to the lagging quality of Russian machinery. U.S. farm equipment is 4 times more efficient than the Russian equivalent in terms of horsepower, said Alexei Melnikov, last month at an economic conference in Belokurikha.

Vadim Kovrizhkin, government relations director at Novoye Sodruzhestvo Holding, who said the blueprint was the result of lobbying by the industry, welcomed the cabinet's intent to improve conditions for leasing. "Peasants don't have the money" to buy machinery, Kovrizhkin said. AIW

# CSI Wireless Revenue Flat for Year-End 2005

CSI Wireless, the Calgary-based designer and manufacturer of advanced wireless and GPS products, including Outback GPS and auto-steer products, reported on March 7 that its revenues remained flat during 2005 compared with 2004.

For the year ended December 31, CSI reported revenues of $75.1 million, as compared to $74.5 million in 2004. The company experienced growth of 8% in both of its core businesses — Hemisphere GPS and Fixed Wireless — relative to 2004. However, as revenues are denominated in U.S. dollars (a 7% average decrease due to the exchange rate during '05), the actual reported revenue growth in Canadian dollars was nominal for both divisions.

"2005 turned out to be a challenging year financially for CSI Wireless," says Stephen Verhoeff, CSI's president and CEO. "However, the strategic changes that we have implemented in 2005 position the company to generate long-term value. The acquisition of the Outback business in the second quarter solidified our position in the GPS agricultural guidance markets. This market has significant global growth potential, and we've seen recent market strengthening following a soft 2005."

"The Outback acquisition, completed in April 2005, was strategically important for CSI. Related inventory accounting principles temporarily impacted gross margins in 2005 and early 2006, but the acquisition ultimately improves CSI's gross margins significantly, and this will be evident in 2006," says Verhoeff.

For 2005 the company's GPS revenues were $32.7 million vs. $32 million in 2004, and Fixed Wireless revenues were $42.4 million vs. $42.5 million in 2004.

"Our fourth quarter and 2005 results are not indicative of our future financial performance," said Verhoeff. "Telematics discontinuance charges impacted the fourth quarter of 2005, however, the decision to divest Telematics will remove significant annual losses. In addition, while the Outback business was acquired toward the end of its strongest selling season, and as a result those sales were not included in our 2005 results, they will be in 2006 and beyond."

CSI held cash at December 31, 2005 of $12.6 million compared to $10.3 million at the end of 2004. "Despite the losses incurred in 2005, the company was able to maintain strong cash management principles," says Cameron Olson, CSI chief financial officer. "As a result, our cash position remains strong heading into 2006."

For 2005, the company reported consolidated gross margins of 29% in 2005, a decrease from 33% in 2004. A temporary decrease in GPS margins in 2005 resulted from an inventory accounting issue arising from the company's acquisition of the Outback business from RHS, Inc.

> "The acquisition of the Outback business solidified our position in the GPS agricultural guidance markets. This has significant global growth potential, and we've seen recent market strengthening following a soft 2005..."

Hemisphere GPS' gross margins were 46% in 2005, a decline from 51% in 2004. Margins for sales to non-agricultural markets showed improvement in 2005 relative to 2004. However, margins on sales to agricultural markets declined during the year, primarily as a result of the accounting issue described earlier.

On the other hand, margins for their wireless products were 16% in 2005 compared to 19% in 2004.

The acquisition of Outback last April from RHS was followed by several other moves designed to further solidify Outback's strong position in the farm GPS and auto-steer markets.

- The combined GPS business was re-branded as Hemisphere GPS.
- CSI's Hemisphere GPS division introduced a proprietary chipset and new Crescent receiver technology. The proprietary chipset establishes the foundation for a receiver product line that Hemisphere GPS is launching under its new Crescent brand name.
- Hemisphere GPS established a strategic partnership with Claas KGaA mbH, one of the world's largest farm machinery manufacturers, to design and supply high-performance GPS receivers and auto-steering systems for use throughout CLAAS product lines, including tractors.
- Hemisphere GPS achieved a sales milestone by selling more than 2,000 of its Outback eDrive and Satloc GPSteer automated steering systems for tractors and other self-propelled agricultural equipment. The company introduced its two auto-steering products in North America in early 2004, and in South America, Europe and Australia during 2005.
- CSI's Hemisphere GPS division acquired the business assets of Del Norte Technology, Inc. for $940,000. Del Norte, with 20 years experience designing and manufacturing specialized GPS products for the aerial guidance market — primarily crop dusting or aerial spraying — had sales of $1.7 million in '05. AIW

## Montana Tractors Aiming High

Rodney Miller, CEO, Montana Tractors, told *Ag Industry Watch* that in 2005, Montana's first full year of operation, the firm notched sales of $64 million on 3,300 tractors shipped via a network of 275 dealers. For 2006, he says the plan calls for $128 million in sales on 6,200 tractors with an increase in the number of dealers to 400. "We have a plan to do this," says Miller, noting the firm's 30 branded implements and loaders and dramatic number of new product launches and new marketing programs that have been created for dealers. "We intend to be a top 5 tractor manufacturer in the U.S. by 2010." AIW

# South Africa's Largest Equipment Distributors Set to Combine Forces

Two of South Africa's largest independent agricultural machinery distributors selling the Case and New Holland lines are preparing to join forces.

Subject to regulatory approval, CSE Equipment Co. will acquire its competitor, New Holland SA, to form a business to handle all CNH Global brands in both agriculture and construction.

CSE's agricultural equipment arm, Northmec, and New Holland SA will continue to run as separate entities as far as customers are concerned, says CSE Equipment CEO Tony Sinclair, but will benefit from combined backroom support.

"This acquisition will broaden CSE's specialized service to an extended customer base and will significantly improve the efficiencies of both companies," he says. "It's a positive move for the agricultural industry, which is currently undergoing enormous change, resulting in necessary consolidation of the equipment market in South Africa."

Since 2004 — when South Africa's tractor market grew by 22% to 5,280 units over the prior year, combine sales shot up by 48% and baler sales increased 67% — the market has slowed.

According to the South African Agricultural Machinery Assn., 2005 tractor sales fell by at least 11%, combines more than 30%. This stems largely from an over-supply of maize from an exceptional harvest that resulted in record low grain prices (below the cost of production), rising farm debt and reluctance among farmers to plant maize again.

CSE Equipment Co., which is owned by Invicta Holdings, an investment management company with sales of $324 million, holds franchises for Case earthmoving machinery and New Holland backhoes.

The Northmec agricultural operation handles Case IH distribution through 10 retail outlets plus another 42 independent dealers. It claims 8-9% of the South African tractor market, with a more substantial share of the big horsepower sector, and around 50% of all combine harvester sales. AIW

# U.S. Manufacturers Export $6 Billion, 15% Gain From Europe

U.S. exports of agricultural-related machinery recorded a 15-percent gain in 2005 to total $6.6 billion, led by strong sales to the European marketplace, according to data released in March by the Assn. of Equipment Manufacturers, which produces a quarterly "global markets" report consolidating U.S. Commerce Department data. This is the fourth consecutive year of gains in exports of farm equipment, although the rate of growth is down slightly compared to the previous year.

Exports of U.S.-made farm equipment to Europe totaled $2.3 billion in 2005, a 37% increase compared to 2004. Exports to Canada increased 17%to total $1.9 billion. Asia recorded a 10% gain as it took delivery of $535 million worth of American-made agricultural machinery.

Exports were flat to South America, with its purchases of $400 million a 1% increase compared to the previous year. Exports to Central America dropped 4% to total $615 million.

Australia/Oceania took delivery of $640 million worth of American-made farm machinery, a 5% decline, and exports also dropped 7% to Africa to $167 million for 2005.

The top 10 buyers of American-made farm equipment in 2005 were (1) Canada — $1.9 billion, up 17%; (2) Australia — $577 million, down 6.5%; (3) Mexico — $469 million, down 11%; (4) France — $341 million, up 14%; (5) Germany — $341 million, up 32%; (6) United Kingdom — $276 million, up 27%; (7) Russia — $168 million, up 126%; (8) Netherlands — $153 million, up 105%; (9) Belgium — $147 million, up 3%; (10) Brazil — $140 million, up 23%). AIW

## Farm Equipment Industry Notes & Newsmakers

**Doug Durand** has been named director of **AGCO** Corporate Marketing and Brand Communications Worldwide, a newly created position. His responsibilities include marketing communications strategies and execution worldwide for all AGCO brands.

**Wendy L. Morris** has returned to **Morris Industries, Ltd.,** Saskatoon, Saskatchewan, as president and CEO.

**Argo Tractors**, a unit of Argo S.p.A, has opened its new parts and distribution center in Norcross, Ga., following the consolidation of McCormick Tractors International, Ltd. and Landini USA.

**Case IH** kicked off production of its redesigned MX-Series Magnum-model farm tractors at its plant in Racine, Wis. The new Magnum line-up, which includes four new models, replaces Case IH's existing line-up. The top-of-the-line MX305-model is powered by new 9.0-liter Tier III diesel engine that generates 255 PTO hp.

**Deere & Co.** launched production in February of its new compact utility-type tractors at an Augusta, Ga., assembly plant. The 3203-model is powered by Tier II compliant, Yanmar 3-cylinder TNV Series diesel engines that generates 32 hp.

**Kubota Corp.** opened its newest manufacturing facility for producing tractor implements in Jefferson, Ga., on February 10. The new 400,000 square-foot facility is being operated as Kubota Industrial Equipment Corp. Initially, the new facility will employ about 500 people to produce 70,000 tractor implements once it is fully operational.

**CNH Global N.V.,** Lake Forest, Ill., has begun offering optional equipment protection plans to purchasers of its agricultural and construction machinery through its finance unit, CNH Capital. The firm said the protection plans would be sold through its 2,600 ag and construction equipment dealers. The new protection plans may be purchased at the time of sale, at any point during the base warranty period and after the base warranty expires. Options range from base protection of the power train, up to the full machine.

# U.S. Tractor Sales 'Up and Down,' Canadian Market Still Strong

February proved to be an "up-and-down" month for the U.S. sales of tractors, according to a March 10 report from the Assn. of Equipment Manufacturers. Canadian sales for the month demonstrated much the same trend but to a much more significant degree.

While U.S. sales of row-crop tractors fell 14.5% during the month compared to February 2005, sales of compact tractors (under 40 hp) rose 6.4%, utility tractors (40-100 hp) jumped 7.4% and 4WD units skyrocketed by 49.7% compared with February '05. Total U.S. tractor sales for the month of February came in 5.1% higher than February '05.

On a year-to-date basis, the results were less dramatic. On this basis, total 2WD tractors grew 0.4% and 4WD machines rose 8.2%.

The breakdown of total tractor sales year-to-date shows: compact tractors +2.8%; utility tractors +4.3%; row-crop tractors –17.6%.

The February sales of combines rose 2% in U.S. compared with the same period last year, but are down 2.3% on a year-to-date basis.

The Canadian figures for February sales came in much stronger but followed much the same path. Total tractor sales were up 16.2% compared with February of '05 and rose 17.7% on a year-to-date basis.

The February '06 breakdown of tractor sales in Canada on a same-month basis was as follows: compact tractors +27%; utility tractors +17.7%; row-crop tractors –6%. Total 2WD sales for the month jumped 14.1% and climbed 16.8% year-to-date.

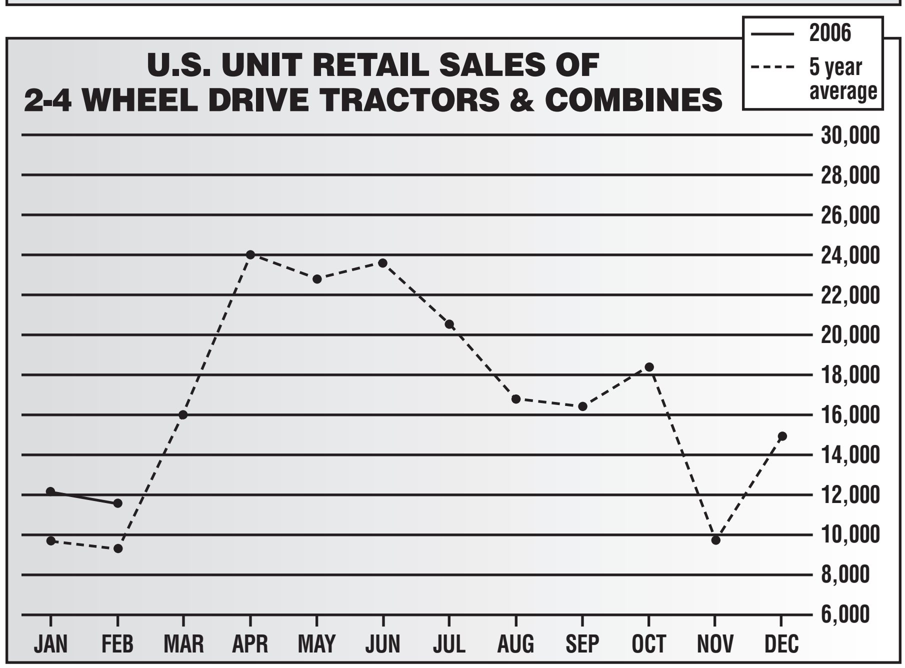
In terms of equipment inventories, David Bleustein, industry analyst for UBS, reports, "Inventories of small tractors, utility tractors, row-crop tractors and combines are above year-ago levels, while inventories of 4WD are below year-ago levels. Given our view of deteriorating farm equipment demand, we expect manufacturers to focus on reducing field inventories in 2006." AIW

## FEBRUARY U.S. UNIT RETAIL SALES

| Equipment | February 2006 | February 2005 | Percent Change | YTD 2006 | YTD 2005 | Percent Change | January 2005 Field Inventory |
|---|---|---|---|---|---|---|---|
| **Farm Wheel Tractors-2WD** | | | | | | | |
| Under 40 HP | 6,132 | 5,762 | +6.4 | 11,401 | 11,091 | +2.8 | 61,149 |
| 40-100 HP | 4,097 | 3,767 | +7.4 | 8,652 | 8,295 | +4.3 | 30,639 |
| 100 HP Plus | 1,037 | 1,207 | -14.5 | 2,729 | 3,310 | -17.6 | 6,134 |
| **Total-2WD** | 11,211 | 10,736 | -4.4 | 22,782 | 22,696 | +0.4 | 97,922 |
| **Total-4WD** | 238 | 159 | +49.7 | 460 | 425 | +8.2 | 831 |
| **Total Tractors** | 11,449 | 10,895 | +5.1 | 23,242 | 23,121 | +0.5 | 98,753 |
| **SP Combines** | 254 | 249 | +2.0 | 590 | 604 | -2.3 | 1,239 |

## FEBRUARY CANADIAN UNIT RETAIL SALES

| Equipment | February 2006 | February 2005 | Percent Change | YTD 2006 | YTD 2005 | Percent Change | January 2005 Field Inventory |
|---|---|---|---|---|---|---|---|
| **Farm Wheel Tractors-2WD** | | | | | | | |
| Under 40 HP | 259 | 204 | +27 | 536 | 446 | +20.2 | 3,963 |
| 40-100 HP | 346 | 294 | +17.7 | 737 | 596 | +23.7 | 2,588 |
| 100 HP Plus | 171 | 182 | -6 | 329 | 329 | 0.0 | 1,444 |
| **Total-2WD** | 726 | 680 | +14.1 | 1,602 | 1,371 | +16.8 | 7,995 |
| **Total-4WD** | 28 | 12 | +133.3 | 57 | 38 | +50 | 172 |
| **Total Tractors** | 804 | 692 | +16.2 | 1,659 | 1,409 | +17.7 | 8,167 |
| **SP Combines** | 49 | 42 | +16.7 | 84 | 104 | -19.2 | 443 |




—*Assn. of Equipment Manufacturers*

# Deere First Quarter Earnings Sets Record

Despite ag equipment sales slipping by 6% in the first quarter of its fiscal period, Deere & Co. reported record earnings for the period in late February. The falloff in ag sales was offset by an 18% jump in construction and forestry equipment and a 20% increase in commercial and consumer equipment sales.

Sales of ag equipment were hurt in part by a tough comparison to the previous year, which was one of the best ever.

In all, the company's earnings grew by 6%. Deere spokesman Ken Golden said the company posted its best-ever sales and earnings for a first quarter, besting the record set last year.

Deere posted net income of $235.9 million for the quarter ended January 31. The earnings outperformed last year's record results of $222.8 million. Sales and revenue increased 7% in the quarter to $4.2 billion, up from $3.935 billion a year ago.

Robert Lane, Deere's chairman and CEO, attributed the improved performance to positive customer demand for the new product lineup as well as a continuing focus on operating efficiency. In a news release, he said "Our rigorous management of operating costs and asset levels is helping sustain strong financial performance. We're continuing to attract new customers worldwide who value the productivity and precision that our offerings deliver."

Growing demand for farmers' products, as well as the outlook for farm cash receipts — though still lower than last year's — prompted Deere to improve its sales forecast for ag equipment. Previously, Deere had forecast ag sales to decline 5-10% over the year. "Now we're saying down 5%. It's a modest improvement," Golden said. "It's an improved picture of where we thought we'd be 3 months ago."

Across all its equipment lines, Deere is forecasting an increase in net sales of 3-5% for the year. Previously, it expected an increase of 1-3%, he added.

On February 14, Deere announced that it would earn $1.7 billion for all of fiscal 2006. On February 23, it reduced its profit outlook to $1.65 billion, saying that it intended to repurchase $500 million of its outstanding debt.

Deere also cut its fiscal 2006 second-quarter profit outlook for the same reason. The company said it now expects to earn a narrower $675-700 million during the second quarter of fiscal 2006 compared with a higher $725-750 million projected a week earlier.

On March 9, the company reported that its February 23 offer by the firm to buy back $500 million of its debt securities had netted notes valued at $646.2 million.

Deere again said it would decide by March 22 exactly how much of each of the five classes of debentures it would repurchase.

Golden said Deere "still is headed toward what will be a record year," in part because of its sale of John Deere Health Care, which was announced in December. The sale to United Healthcare of Minneapolis is expected to close during the current quarter. It will boost profits by $225 million after taxes.

Baird analyst Robert McCarthy, says the Deere's fiscal 2006 outlook "appears to be reasonably balanced."

On the ag side, which made up 54% of Deere's fiscal '05 sales and 53% of its operating income, McCarthy says, "A modest increase to Deere's forecast reflects a slightly stronger forecast in North American sales offset by a weaker South American outlook. We believe Deere's flat-to-down 2% revenue growth forecast (previously down 2-4%) reasonably incorporates the forecast declines in North American farm cash receipts, net income and pervasive industry forecasts for modest agricultural equipment unit sales declines.

This, along with the potential adverse farmer sentiment related to government subsidies — from both the U.S. 2007 farm bill and European implementation of Common Agricultural Policy — and another weak South American outlook, is balanced by the positive impact of Deere's new product introductions." AIW

# Gehl 4th Quarter Profit Doubles as Sales Rise 15.7%

On February 27, Gehl Co. reported that its profits soared in the fourth quarter as sales jumped 15.7%, more than doubling its revenues from a year ago. Based in West Bend, Wis., Gehl manufactures Gehl and Mustang-branded skid steers, telescopic handlers and other equipment used in ag and construction.

The company's backlog of unfilled orders also skyrocketed by more than 180% $186.3 million at the end of last year.

Gehl earned $6.2 million during the final quarter on sales of $108.7 million. A year ago, it earned $2.9 million from revenues of $93.9 million.

For all of 2005, Gehl's profit soared to $21.8 million on sales of $478.2 million. This compares to a year-ago gain of $13.4 million from sales of $361.6 million.

Its cash on hand at the end of last year fell to $4.8 million from $5.3 million one year earlier. Inventory valuation increased to $43.6 million from $38.9 million and the value of its outstanding long-term debt was cut to $52.1 million from $69.5 million during the same periods, reflecting an improved balance sheet.

Baird analyst Robert McCarthy says, "Gehl has continued to outperform the industry via new product launches, leveraging its distribution capacity with product line expansion and cross-selling compact construction machines through its Gehl and Mustang dealers and ag dealers.

"A sizable plant rationalization program, projected to reduce overall headcount by 10% and yield annual cost savings of $4-4.5 million, has been completed and provides significant operating leverage to stronger end-market demand conditions. A small, but expanding Internet-based equipment attachments business is also being expanded to augment growth," he says.

Based on forecasts for compact equipment, Gehl expects '06 sales of $510 million, a 7-9% increase over '05.

"Our markets are still showing signs of solid growth, although perhaps not as robust as in 2004 and 2005," says William Gehl, chairman and CEO. AIW

A Special Management Report From

Ag Industry Watch

An *Ag Industry Watch* Staff Report

# The Agricultural Equipment Industry in Europe

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- The Netherlands
- United Kingdom

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## VALUE OF AGRICULTURAL MACHINERY IN THE EUROPEAN UNION (IN MILLION OF EUROS)

| Country | Production 2003 | Production 2004 | Exports 2003 | Exports 2004 |
|---|---|---|---|---|
| Germany | 3939.9 | 4531.5 | 2806.2 | 3425.2 |
| Italy | 3730.6 | 3950.0 | 2552.8 | 2759.3 |
| France | 2700.0 | 3140.0 | 1556.0 | 1780.0 |
| United Kingdom | 1785.2 | 1720.3 | 1175.0 | 1115.7 |
| Austria | 851.9 | 824.0 | 539.0 | 539.2 |
| Denmark | 757.0 | 750.0 | 455.2 | 465.6 |
| Spain | 526.8 | 530.0 | 300.8 | 297.0 |
| Netherlands | 541.1 | 520.0 | 776.2 | 776.0 |
| Finland | 565.9 | 504.0 | 366.2 | 319.3 |
| Belgium | 585.9 | 499.0 | 484.0 | 438.0 |
| Sweden | 440.0 | 420.0 | 376.9 | 353.4 |
| Ireland | 140.0 | 150.0 | 100.4 | 106.0 |
| Portugal | 80.0 | 87.0 | 15.4 | 18.4 |
| Greece | 40.0 | 45.0 | 18.3 | 25.6 |
| EU 15* | 16684.1 | 17670.7 | 4652.4 | 4889.3 |
| EU 10 (as of 2004)* | 1800.0 | 2000.0 | 603.7 | 712.4 |
| EU 25* | 18484.1 | 19670.7 | 3917.9 | 4335.8 |

| Country | Imports 2003 | Imports 2004 | Market Volume 2003 | Market Volume 2004 |
|---|---|---|---|---|
| Germany | 1530.7 | 1418.6 | 2664.3 | 2524.8 |
| Italy | 673.5 | 673.5 | 1851.2 | 1878.0 |
| France | 2392.0 | 2650.0 | 3536.0 | 4010.0 |
| United Kingdom | 1104.3 | 1199.6 | 1714.5 | 1804.2 |
| Austria | 368.9 | 364.9 | 681.8 | 649.7 |
| Denmark | 538.2 | 543.6 | 840.0 | 828.0 |
| Spain | 910.2 | 914.7 | 1136.2 | 1147.7 |
| Netherlands | 521.3 | 533.5 | 286.2 | 277.5 |
| Finland | 194.4 | 175.9 | 394.1 | 360.6 |
| Belgium | 731.0 | 851.0 | 832.9 | 912.0 |
| Sweden | 402.0 | 399.6 | 465.1 | 466.1 |
| Ireland | 278.21 | 309.2 | 317.8 | 353.2 |
| Portugal | 186.3 | 212.4 | 250.9 | 281.0 |
| Greece | 133.6 | 195.2 | 155.3 | 214.6 |
| EU 15* | 2077.7 | 2207.8 | 15126.1 | 15707.3 |
| EU 10 (as of 2004)* | 1029.5 | 1131.6 | 2225.8 | 2419.1 |
| EU 25* | 1691.7 | 1822.4 | 17351.9 | 18126.5 |

**excludes trade within the EU*
*Sources: CEMA, Eurostat, VDMA estimates*

# TABLE OF CONTENTS



# TABLES & CHARTS



## *Information Sources*

VDMA — The German Agricultural Machinery Assn. • Farmers Weekly • Climmar — Assn. for Trade & Services of Agricultural Machinery • U.S. Commercial Service of the Dept. of Commerce • Sygma Economique • UNACOMA — National Union of Construction and Agricultural Machinery

## *Explanatory Notes*

Most of the values shown in the original references for this report were shown in Euros. These were converted to U.S. dollars at an exchange rate of 1.2 (e.g. Euros x 1.2 = USD)

# EUROPEAN UNION MEMBER AND CANDIDATE COUNTRIES – 2005

- Austria
- Belgium
- Cyprus
- Czech Republic
- Denmark
- Estonia
- Finland
- France
- Germany
- Greece
- Hungary
- Ireland
- Italy
- Latvia
- Lithuania
- Luxembourg
- Malta
- Poland
- Portugal
- Slovakia
- Slovenia
- Spain
- Sweden
- The Netherlands
- United Kingdom

**Candidate Countries**

- Bulgaria (2007)
- Croatia
- Former Republic of Yugoslavia
- Romania (2007)
- Turkey

# The Agricultural Equipment Industry in Europe

As a trade bloc, the European Union (EU) and its current 25 member states is the world's largest economy. Though the largest individual manufacturers of ag equipment, most notably tractors, are based in the U.S. (Figure 1), the EU ranks first in the world in terms of the total market for the production of farm machinery. According to statistics released by the VDMA Agricultural Machinery Assn. in Frankfurt, Germany, the production volume of agricultural equipment produced in the EU in 2004 reached nearly $24 billion dollars.

According to the VDMA, some 1,200 facilities in the EU produce ag equipment, although fewer than 400 of those firms employ more than 20 people. Total employment in this sector is about 135,000. It is estimated that 2% of these equipment manufacturers are responsible for 60% of equipment volume produced in EU countries.

The 25 countries that are currently members of EU are listed on p. 11, as well as the 5 countries that are candidates to join the EU in the near future.

The major agricultural equipment producing countries of the EU include Germany, which accounts for 23% of total production, Italy 20% and France 16%. More than 75% of the ag equipment manufactured in Europe is sold within the EU itself. The largest export markets for EU-produced equipment include North America and the Commonwealth of Independent States (CIS).

Only six Western European countries manufacture farm tractors, while Spain assembles them (Table 1). In 2004, equipment makers in these countries produced nearly 215,000 tractors. While the production of tractors in the EU grew by 5% in 2004, the longer-term prospects for production in the U.K. are less clear as AGCO (Massey Ferguson) departed England in 2003 for France and Brazil. The resumption of production of McCormick tractors by the Argo group of Italy in Doncaster, England, in 2005, though, provided some good news.

Statistics for the manufacture of farm machinery in Central and Eastern European countries are not reliable at this time. Nonetheless, this region has some significant producers of tractors and other implements required by local farmers.

In addition to the major tractor makers throughout Europe, the con-

**TABLE 1. TRACTOR PRODUCTION IN WESTERN EUROPE (IN UNITS) 2003 – 2004**

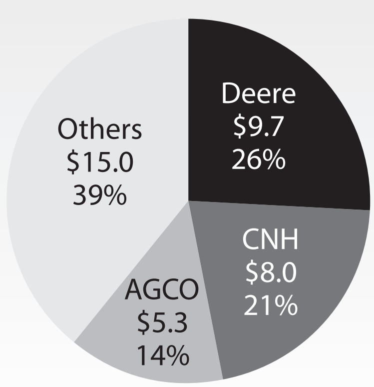
| | 2003 | 2004 | % Change |
|---|---|---|---|
| Italy | 79,847 | 78,141 | -2.1% |
| Germany | 51,407 | 59,236 | 15.2% |
| U.K. | 30,408 | 29,138 | -4.2% |
| France | 22,490 | 26,530 | 22.4% |
| Austria | 8,509 | 9,856 | 15.8% |
| Finland | 10,928 | 9,691 | -11.3% |
| Spain | 1,039 | 1,027 | -1.2% |
| **Total** | **204,628** | **214,619** | **4.9%** |

**TABLE 2. MAJOR EUROPEAN FARM MACHINERY MANUFACTURERS (OTHER THAN TRACTORS)**

| Company | Country | 2004 Net Sales (000 $) |
|---|---|---|
| Kverneland | Norway | $604 |
| Kuhn | France | $556 |
| Amazone | Germany | $240 |
| Krone | Germany | $206 |
| Lely | Netherlands | $190 |
| Exel | France | $170 |
| Hardi | Denmark | $162 |
| Pottinger | Austria | $154 |
| Alo | Sweden | $151 |
| Grimme | Germany | $126 |
| JF-Stoll | Denmark | $138 |
| Maschio | Italy | $108 |
| Kongskilde | Denmark | $118 |
| Lemken | Germany | $110 |
| Alamo | U.K. | $95 |
| Vaderstad | Sweden | $74 |

*Source: Farmers Weekly*

**FIGURE 1. ESTIMATED AG EQUIPMENT SALES BY MANUFACTURER**
**(Billions $)**




*Foresight Research Solutions, LLC*

tinent also boasts several major manufacturers of farm implements. Table 2 shows the largest European producers of non-tractor farm machinery and implements.

## The New EU States

The EU expanded its reach by 10 countries in 2004: Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia. These countries, many of which were part of the former Soviet Union, remain as net importers of farm machinery. Figures 2-3 show the

**FIGURE 2. EXPORTS OF AG MACHINERY OF THE 10 NEW EU MEMBER COUNTRIES (% OF PRODUCTION)**

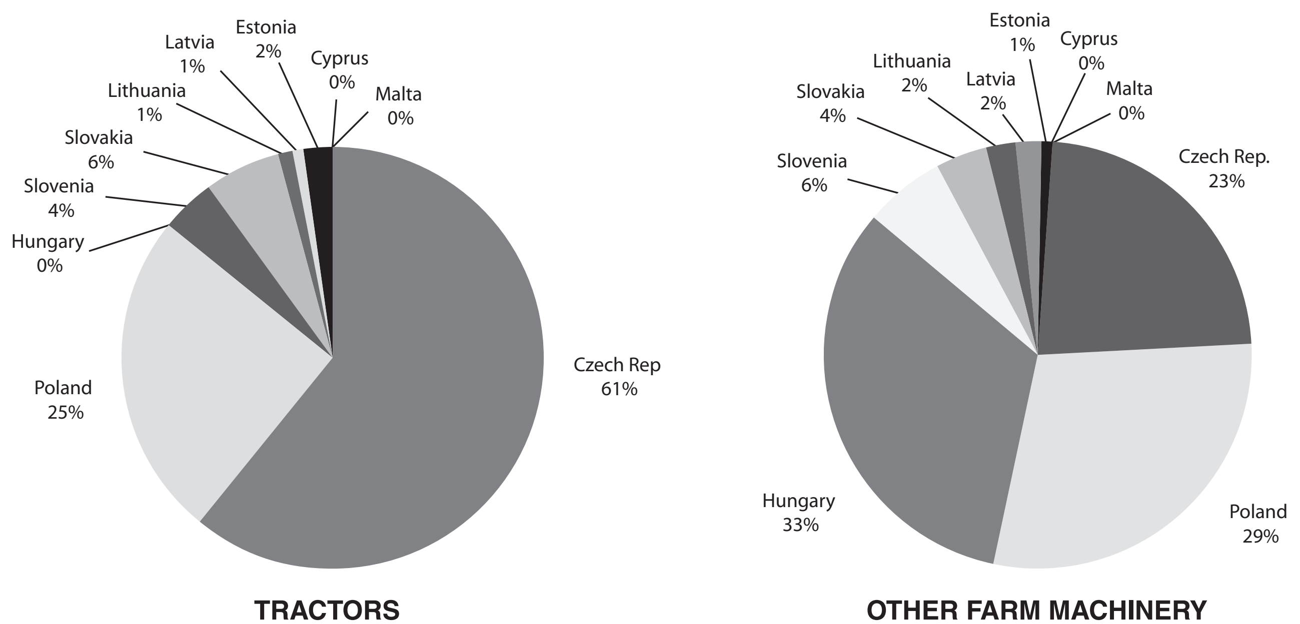
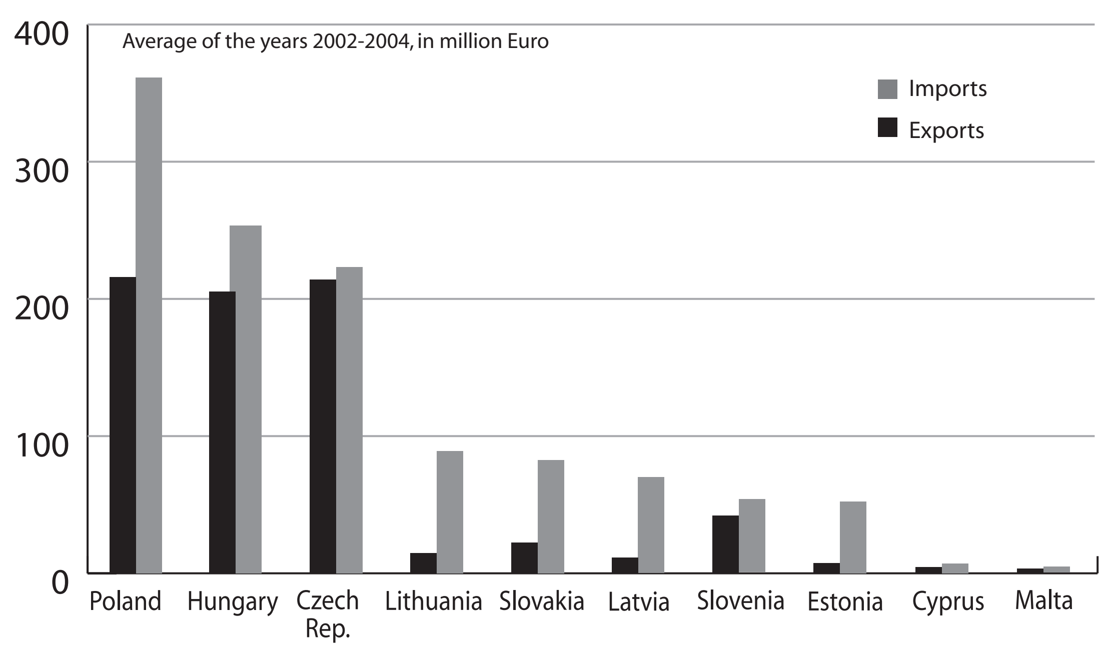



**FIGURE 3. EXPORTS AND IMPORTS OF AG MACHINERY IN THE NEW EU STATES**




*Source: national statistic agencies*

export-import activities for each of the newest members of the EU.

In 2004, the value of the imports to the 10 newest states of the EU was $1.5 billion compared with about $1 billion in exports. Of the exports, comprised mainly of parts and components, $654 million were supplied to the EU 15 countries. More than 80% of this equipment originated from Poland, the Czech Republic and Hungary.

More than one-third of the imports into these countries came from Germany, followed by Italy and Finland. Poland accounted for more than 40% of the total imports coming into the new EU countries.

## Distribution Channels

Unlike the distribution network in the U.S., where equipment manufacturers, in large part, work directly with local dealers, the European model is more heavily dependent upon a regional distributor network. These distributors act as a "middle man" between the equipment manufacturers and the local dealerships. Table 3 shows a breakdown of the 15 EU countries in terms of equipment dealers, farmers per dealer and the relative size of farms.

## Outlook for the EU

It is estimated that the worldwide market for ag equipment is valued at more than $65 billion. EU countries claim about a 40% market share of this global industry. Figure 4 illustrates the market volume of the largest Western European farm equipment producers.

It is expected that the three largest manufacturing nations in the EU — Germany, Italy and France — will see an increase of about 6% in sales during 2006. According to the VDMA, the outlook for Germany calls for an increase of 5%, which would correspond to a value of $5.7 billion. "For the first time, the stimulus comes from the domestic market again this year, whereas the increase in the export business is weaker after years of significant growth," reports Bernd Scherer, managing director of VDMA.

Italy's manufacturers expect a significant rise in sales of 8% based largely on growth of export products. Sales by farm machinery manufacturers in France exceeded the level of the previous year by 7% as their export share grew to 62%. Despite stagnant markets in other Western European states, growing exports to Central and Eastern European countries are expected to boost sales of ag equipment by 5% throughout the EU during the coming year.

Overall, the European agricultural machinery industry continues to strengthen its position throughout the European continent as well as in North America, even with disadvantages resulting from the exchange rate. The export of ag equipment for selected countries is shown in Figure 5.

## Overview of EU Markets

Following an overall increase of 4% in 2004, sales of ag equipment in the EU in 2005 slowed slightly. As a result of increased capital spending in the new member states, however, a nominal increase of 3% is projected for the EU 25 in '06.

The biggest volume gains in the near term are expected to come in the manufacture and sales of harvesting

### TABLE 3. STATISTICAL RATIOS OF AG DEALERS, FARMS AND FARM SIZE

**2005 WESTERN EUROPEAN AGRICULTURAL DATA**

| | Dealers | Farmers | Employees | Average Farm Size (HA) | Average Farm Size (Acres) | Farmers Per Dealer | Employees Per Dealer |
|---|---|---|---|---|---|---|---|
| Germany | 4750 | 388,500 | 34,400 | 43.8 | 108.2 | 81.8 | 7.2 |
| Austria | 410 | 170,000 | 3,100 | 25.0 | 61.8 | 414.6 | 7.6 |
| Belgium | 350 | 52,050 | 1,450 | 25.4 | 62.8 | 148.8 | 4.1 |
| Denmark | 203 | 46,502 | 3,105 | 56.5 | 139.6 | 229.1 | 15.3 |
| France | 1,100 | 590,000 | 24,000 | 45.0 | 111.2 | 536.4 | 21.8 |
| Hungary | 860 | 219,000 | 6,600 | 18.0 | 44.5 | 254.6 | 7.7 |
| U.K. | 2000 | N/A | 20,000 | N/A | N/A | N/A | 10.0 |
| Ireland | 250 | 135,000 | 3,200 | 35.0 | 86.5 | 540.0 | 12.8 |
| Italy | 2,200 | 2,300,000 | 7,000 | 5.0 | 12.3 | 1045.5 | 3.2 |
| Luxembourg | 20 | 1,481 | 190 | 60.0 | 148.3 | 74.05 | 9.5 |
| Netherlands | 800 | 100,000 | 6,000 | N/A | N/A | 125.0 | 7.5 |
| Portugal | 650 | 416,000 | 5,000 | 9.3 | 22.9 | 640.0 | 7.7 |
| Sweden | 150 | 76,800 | 1,875 | 35.0 | 86.4 | 512.0 | 12.5 |
| Switzerland | 20 | 71,000 | 511 | 15.3 | 37.8 | 3550.0 | 25.55 |
| Czech Rep. | 320 | 8,500 | 2,190 | 150.0 | 370.7 | 26.6 | 6.8 |
| **TOTALS** | **14,083** | **4,574,833** | **118,621** | **40.25384615** | **99.46725385** | **324.8479017** | **8.42299226** |

machines and combines. While these sales were depressed during the past few years, demand began to rise in '05 as a result of larger harvest volumes.

For most European markets, the sales of new combines grew only slightly during the 2004-05 season. The number of combines sold in this period was about 6,800 units, somewhat above sales levels of the year before. Only in the U.K., Spain and Italy did the sales volume fall significantly below the volume of the previous year. On the other hand, the market for this equipment in Germany increased by 19%, which helped compensate for poor years in 2003 and 2004.

**FIGURE 4. MARKET VOLUME OF THE BIGGEST WESTERN EUROPEAN MARKETS**

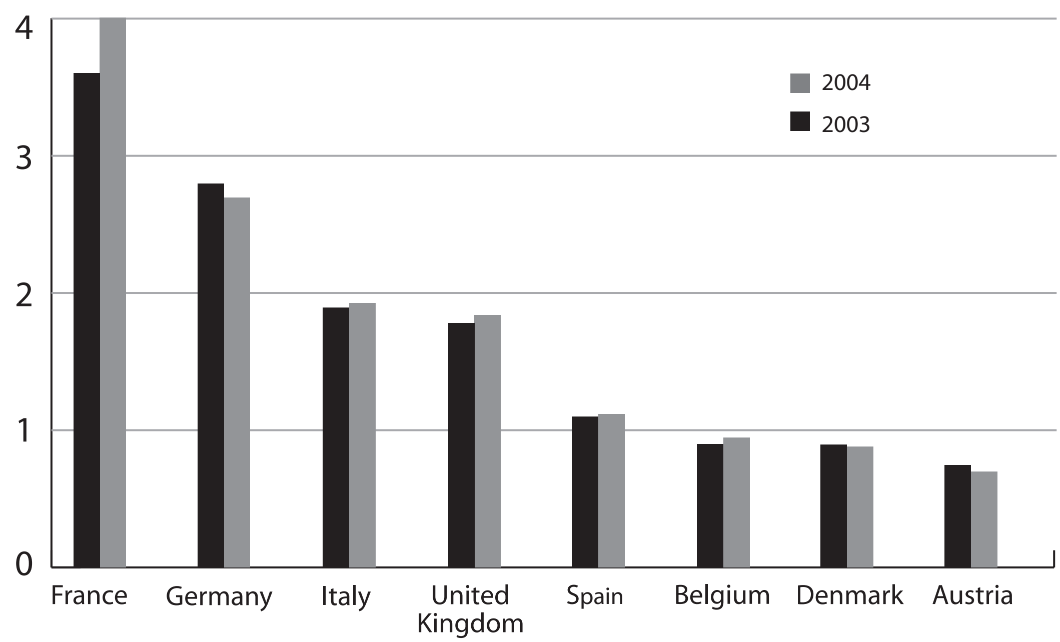
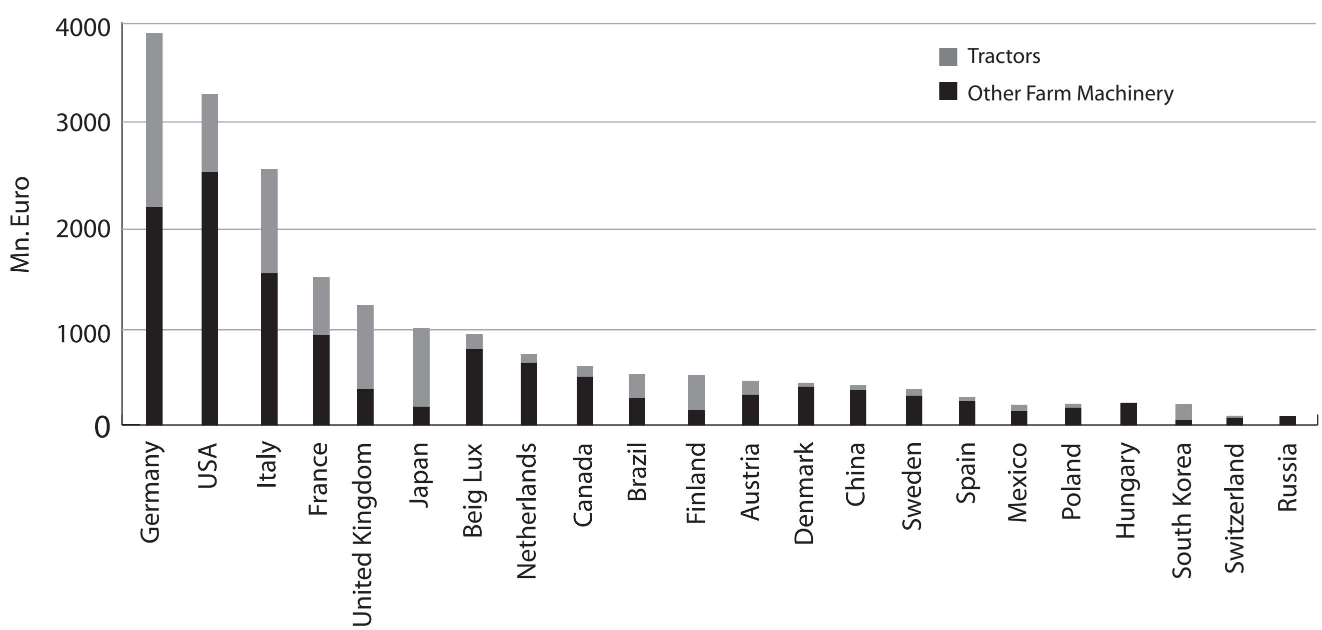



**FIGURE 5. EXPORTS OF AG MACHINERY OF SELECTED COUNTRIES — 2003**



Other forage harvesting equipment that experienced market growth in '05 included round balers (6%), big balers (3%) and mowers/conditioners (1%). Increased sales of harvesting equipment in Germany were due in large part to the construction of new biogas plants, resulting in a relatively stable market for much of Western Europe. This is helping to offset a 15% decline in sales of this equipment in other areas of Europe.

As for the Western European tractor market, a decrease of 3% to 176,500 units is predicted for 2006. Sales of tractors in the range of 50 hp or larger are expected to reach 153,000 units. At this level, the market is considered to be stagnant, remaining at essentially the same level of the previous year. French tractor makers are expected to see the largest dropoff due to declines in shipments to the U.K., the Netherlands and Spain. So far, the Italian market has remained stable, and significant growth in Germany will only compensate for the overall reduction in the EU.

With the exception of combines and harvest equipment, sales of other farm machinery are not expected to fare as well in 2006 as it did in '05. No noticeable growth trend is seen for any of the other equipment categories, which include machines for tillage, sowing, fertilizing, spraying or that for livestock use. However, it appears that declines in unit sales may be offset by the value of shipments as the result of the growth in machinery size, such as the larger fertilizer spreaders and spraying equipment coming into the market in recent years. As a result, the sales value of these types of equipment in Western Europe are likely to remain at the levels seen in the previous year.

## A Flourishing Market in France

France has the largest market for tractors and agricultural machinery in Europe. According to the U.S. Commercial Service of the U.S. Dept. of Commerce, the French market for ag equipment totaled $4.93 billion in 2004, and represents 25% of the total European ag equipment market and is second only to the U.S. in farm equipment imports on a global level. (Table 4). The U.S. is one of France's top suppliers of farm machinery (along with Germany and Italy), with a share of the current market estimated at 10.6%.

Market figures for 2004 showed an average growth of nearly 13.3% percent over the previous year. Growth in demand came primarily from tractors (5.3% in volume and 7.7% in value), combine harvesters (11.9% in volume) and high-density press balers (37% in volume). This pace is expected to level off slightly over the next 2 years mainly due to global economic uncertainties and farmer anxiety. In addition, the recent increase in steel and gasoline prices is expected to affect sales of new mobile agricultural machinery in coming years, especially tractors.

Production of tractors and other agricultural machinery is heavily concentrated in a few multinational manufacturers. The American firms John Deere, AGCO (Massey Ferguson, Fendt, Valtra), Caterpillar and Case New Holland dominate the domestic scene (Table 5).

In total, the French ag equipment industry is comprised of 205 companies, employing 22,000 people.

As the largest agricultural machinery market within Europe, France always plays a lead role in the overall trends of the industry. Since March 2005, the tractor market there has fallen below the level of the year before. This isn't surprising since tractor sales grew by 5% to 40,000 units in 2004 (Table 6). This was the sec-

**TABLE 4. VALUE OF THE AG EQUIPMENT MARKET IN FRANCE — 2003-04 (IN BILLIONS $)**

| | 2003 | 2004 |
|---|---|---|
| Total Market | $3.6 | $4.9 |
| Total Domestic Production | $3.2 | $3.9 |
| Total Exports | $1.7 | $2.2 |
| Total Imports | $2.7 | $3.3 |
| Total Imports from U.S. | $279 | $344 |

*Source: Sygma Economique*

**TABLE 5. MARKET SHARE OF TRACTOR MAKERS IN FRANCE**

| | 2003 | 2004 |
|---|---|---|
| John Deere | 17.8% | 18.6% |
| New Holland | 16.1% | 14.8% |
| Renault | 15.4% | 13.8% |
| Massey Ferguson | 8.0% | 10.9% |

*Source: Sygma Economique*

**TABLE 6. AG EQUIPMENT PRODUCTION IN FRANCE (NUMBER OF UNITS) – 2004-05**

| | 2003 | 2004 |
|---|---|---|
| Tractors | 38,245 | 40,279 |
| Combines | 1,459 | 1,633 |
| Balers | 5,833 | 6,764 |
| Forage Harvesters | 384 | 419 |
| Mowers/Conditioners | 2,618 | 2,776 |
| Trailers | 25,420 | 24,530 |

*Source: Sygma Economique*

ond highest level ever, exceeded only in 1999. At 37,500 units, 2005 was expected to fall 7% below '04 levels.

While investment in cattle ranching and lawn and garden maintenance is increasing, demand in the intensive livestock and viticulture (vineyards and grapes) segments is diminishing. It is expected that the market value of French ag equipment for all of 2005 was $4.6 billion. This figure is only slightly below the value of equipment sales during the previous year. The forecast for '06 calls for a falloff of 5%.

In line with the general trend in EU markets, sales of farm implements are forecast to drop by 10-15% compared with 2005. In the harvesting machinery segment, however, sales increased last year, except for forage harvester and big baler equipment. The 2004-05 season ended with an increase of 7% (1,754 units) for combines and 15% (6,025 units) for round balers. Mower sales exceeded the level of the previous year by 6%.

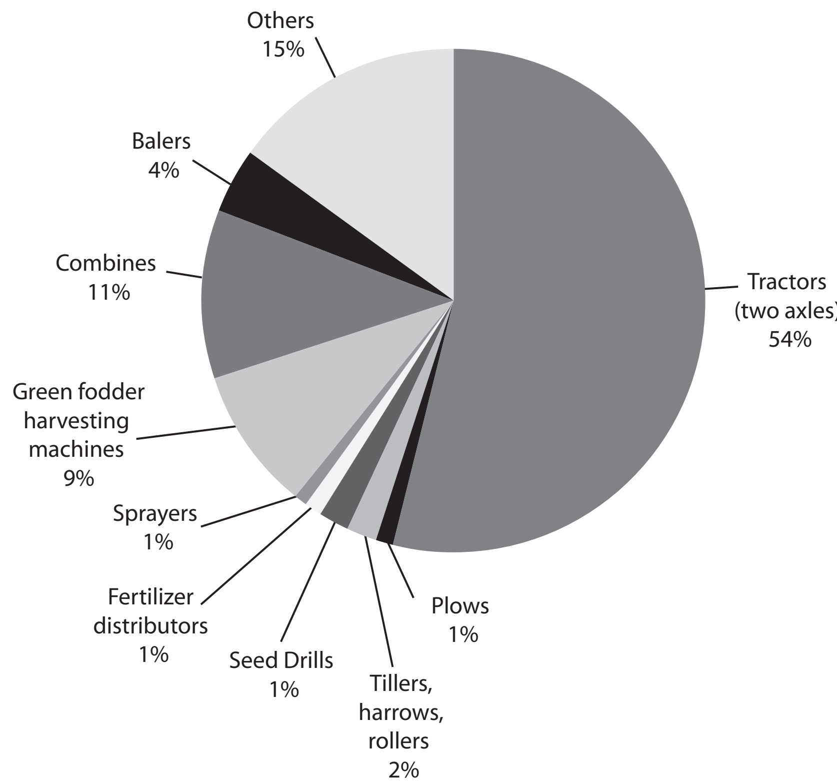
In addition to crop and pricing factors, the insecurity on the part of farmers as to how the new agricultural policy will affect the economics of farming will set much of the direction for the future of France's agriculture industry.

Despite this, several positive factors, such as the rising demand for investment in farm infrastructure, tax incentives and high meat prices, will help stabilize the market for agricultural machinery. Negative factors include the high price of energy and other ag inputs.

Industry analysts expect a leveling off of the agricultural machinery and equipment sector for the next two years. The European Union (EU) reforms of the Common Agricultural Policy (CAP) and the EU enlargement have resulted in uncertainty and in a general reluctance from French farmers to invest.

The reform plan to grant financial incentives to Eastern European Countries that have entered the EU might trigger a fall in the investments in equipment by French farmers and breeders. Cattle farmers and milk producers should be exceptions. Growing foreign competition combined with more stringent hygiene and environmental standards and with lower ovine, beef, meat and milk prices will continue to push cattle breeders and milk producers to further automate operations in 2006 and beyond.

**FIGURE 6. BREAKDOWN OF GERMAN AG EQUIPMENT SALES (by value)**




## An Expanding German Market

Following very weak sales years in 2003 and 2004, the German market bounced back in 2005. By the end of the year, sales of farm machinery had exceeded that of the previous year by 10-15% as farmers and contractors increased their investments. Together with the growth in renewable energy practices, high meat prices and clear political conditions, the stage is set for sustained growth for German ag equipment. Figure 6 illustrates the breakdown of sales of German farm machinery by equipment type. Table 7 shows production figures for 2003-04.

With high crop yields in 2004 allowing for increased spending for equipment, tractor sales in '05 grew

**TABLE 7. AG EQUIPMENT PRODUCTION IN GERMANY (NUMBER OF UNITS)**

| | 2003 | 2004 |
|---|---|---|
| Tractors | 21,869 | 22,143 |
| Combines | 2,205 | 1,874 |
| Balers | 2,192 | 2,022 |
| Forage Harvesters | 341 | 358 |
| Mowers/Conditioners | 11,228 | 10,291 |
| Trailers | 10,369 | 9,140 |

*Source: VDMA*

by 6% to 23,500 units. The sale of the harvesting machines grew considerably, as well.

The rapidly rising demand for combines in East Germany played a major role in the increased sales of harvest equipment last year. Overall, this market segment grew by 29% to 2,228 units. While sales of other German farm machinery also improved in '05, increases were not nearly as significant.

The rising costs of operating inputs are especially threatening to Germany's agricultural industry in '06 as German farmers pay higher taxes on agricultural diesel than producers in neighboring countries.

In terms of total farm income, 2005 would rank as only an "average year" for German farmers. While hog producers benefited from rising prices, dairy farms face strong cost pressures. Not even the good market for beef can compensate for sinking milk prices, which were running at about 31 cents per kg at year's end.

Row-crop farms had a good harvest in 2005. However, feed grain accounted for a large percentage of the production. As a result, farm incomes did not rise in proportion to crop yields. Nonetheless, as German producers seek to improve their productivity, overall investment in new equipment is expected to remain stable throughout 2006.

**TABLE 8. 2005 PRODUCTION AND VALUE OF ITALIAN AGRICULTURAL EQUIPMENT**

| Production | Units (+/- vs. '04) | Tons (+/- vs. '04) | Value (*millions of $*) (+/- vs. '04) |
|---|---|---|---|
| Tractors | 84,500 (+2.3%) | 223,500 (+0.4%) | $2.76 (+2.6%) |
| Incomplete Tractors & Spares | | 75,600 (-2.9%) | $897 (-0.4%) |
| Agricultural Machinery | | 629,000 (+0.4%) | $4.77 (+0.7%) |

**TABLE 9. VALUE OF ITALIAN IMPORTS AND EXPORTS OF AG EQUIPMENT**

| | Imports | % | Exports | % |
|---|---|---|---|---|
| EU-15 countries | $524,463 | –4.8 | $1,378,922 | +9.1 |
| All Europe | $571,330 | –8.2 | $1,818,347 | +10.0 |
| Africa | $207 | –65.2 | $109,011 | –8.7 |
| America | $374,661 | +7.2 | $369,720 | +16.3 |
| Asia | $59,637 | +13.7 | $153,877 | -0.4 |
| Oceania | $1,961 | +83.4 | $69,955 | +10.2 |
| World Total | $669,887 | –5.8 | $2,522,076 | + 9.2 |

*(Value in thousands of dollars and percentage variations are for the same period in 2004)*

**TABLE 10. 2006 OUTLOOK FOR ITALIAN AG EQUIPMENT INDUSTRY**

| | Units | Weight (*tons*) | Dollars (*Millions*) |
|---|---|---|---|
| **Production (1)** | | | |
| Tractors<br>2006 vs. 2005 | 83,900<br>-0.7% | 223,700<br>+0.1% | $2.78<br>+0.7% |
| Agricultural Machinery, Components and Spares<br>2006 vs. 2005 | | 703,000<br>-0.2 | $5.72<br>+0.9 |
| **Exports (2)** | | | |
| Tractors<br>2006 vs. 2005 | 65,250<br>0.4% | 182,000<br>0.8% | $1.56<br>1.2% |
| Agricultural Machinery, Components and Spare<br>2006 vs. 2005 | | 430,500<br>0.6% | $2.89<br>1.6% |

*(1) Figure estimated on retail prices, VAT not included*
*(2) CIF and FOB prices.*

## Exports Keep Italian Manufacturers on Pace

Italian tractor and agricultural machinery makers saw continued growth in both domestic and export markets in 2005 and are expecting slow, steady growth into '06, according to the National Union of Construction and Agricultural Machinery.

Reports from the group indicate that in 2005, the value of tractor production, incomplete tractors, spare parts and agricultural machinery rose to $8.4 billion in '05 compared with $8.3 billion in '04. This represents an increase 1.2% in value compared to 2004.

Table 8 shows the breakdown of the total Italian agricultural equipment market. Italian farm machinery manufacturers report that both exports and imports grew in 2005. Preliminary numbers for the year indicate that the value of exports increased to about $4.4 billion compared with $4.3 billion in '04, up 2.3%.

Expectations for imports suggest ed that there would be an overall decrease in unit shipments and value of the equipment in '05. The totals for imports showed a surplus of about $1 billion, which is lower by 2.9% vs. $1.03 billion in 2004.

Italian analysts say that the '05 trade balance displayed an overall surplus for tractors, incomplete tractors, spare parts and other agricultural machinery of 3.1%. The value of imported ag equipment is estimated at $3.4 billion compared with $3.3 billion in 2004, or +3.9%.

Between January and July 2005, exports increased by 4.4% in weight and 9.2% in value. A detailed breakdown of the results for the 7 months showed that tractors increased by 7.1% in weight and 12% in value. Exports of other agricultural machinery grew by 3% in weight and 7.6% in value. Imports decreased by 9.9% in weight and 5.8% in value.

The value of Italy's imports and exports of tractors and agricultural machinery broken down by geographic area is shown in Table 9.

In terms of export volume, Europe continued to be the largest export market for Italian farm equipment for the first 7 months of 2005, accounting for 72.1% of the total value of exported equipment compared with 71.6% in '04. The Americas followed with a 14.7% share, up from 13.8% in the previous year. Asia's share of Italian exports slipped to 6.1% compared to 6.7% in '04, Africa's share grew to 5.2%, up from 4.3%. Oceania accounted for 2.8% of Italian exports, the same level of the year prior.

Table 10 shows the forecast for Italian ag equipment exports in 2006. A slowdown in exports of tractors is forecast largely due to stagnant demand in Western Europe and the U.S. At the same time, exports are expected to increase to Central and Eastern Europe.

The outlook for the domestic market for tractors is 34,500 machines in 2006 vs. 35,500 in 2005 (-2.8%). For other agricultural machinery, components and spare parts, a decrease of about 0.6% is expected.

## Tough Times in the U.K.

In the United Kingdom, 4 years of growth from previously low levels were followed by a significant falloff in 2005. In the first 9 months of the year, the tractor market shrank by 12.5%, representing a dropoff of 13,000 new registrations by year's end. Through August of '05, sales of other farm machinery fell only by 3% thanks to increased sales of spare parts.

After a dramatic rise in sales of combines in 2004 (Table 11), the market fell back by 15% in '05 to 630 units. The baler market exhibited only a very slight decrease, and the forage harvester market diminished significantly to 114 units. So far, the outlook for the coming months is not markedly improved as U.K. farmers continue to push back their purchasing plans. In general, the cash flow of the farms has fallen in both the row-crop farming and the dairy cattle sector.

**TABLE 11. AG EQUIPMENT PRODUCTION IN THE U.K. (NUMBER OF UNITS) – 2004-05**

| | 2003 | 2004 |
|---|---|---|
| Tractors (over 40 hp) | 14,606 | 14,995 |
| Combines | 640 | 755 |
| Balers | 1,760 | 1,462 |
| Forage Harvesters | 170 | 151 |

*Source: A.E.A.*

## A Mixed Bag for Other EU Markets

The outlook for ag equipment sales in other European countries is a mixed one. Scandinavian markets continue to develop a healthy upward pattern. Like Germany, Denmark expects significant growth in its markets for farm machinery. In Belgium, the market is shrinking, though the demand for machinery is expected to pick up again somewhat by the end of the year. The Dutch market is also incurring heavy declines.

During the past year, the Iberian Peninsula was affected by a major drought as little or no rain fell from the beginning of the year until the harvest. Consequently, investment in new machinery was greatly diminished. Markets in Switzerland and Austria are stable with some possibility of growth in 2006. And in Switzerland, the downward trend of the past several years appears to be ending.

## Potential Abounds in Central and Eastern Europe

Once again, the agricultural machinery market in the new EU countries has showed very healthy development in 2005. For most of these countries, Germany is the main supplier, especially of harvesting machinery. Therefore, German exports are considered a good indication of the market development. In 2005, shipments skyrocketed following 2 years of moderate growth.

From January through August '05, German exports to the 8 new Eastern European EU member countries increased by 42% to $414 million. The Polish market, which absorbed 38% more German agricultural machinery in '05 than in the previous year, accounted for 30% of the German exports to the new EU 10 states.

However, growth was experienced in all of the new EU countries. Comparatively, Slovenia and Hungary, where imports picked up during the last 3 months of the year, exhibited the most moderate growth rates. At least for German farm equipment makers, Russian and Ukraine markets are showing good potential and are developing into solid trade partners. In Romania and Bulgaria, the Special Assessment Program for Agricultural and Rural Development funds for the preparation to EU accession are also exerting a positive influence on investments in the agricultural sector.

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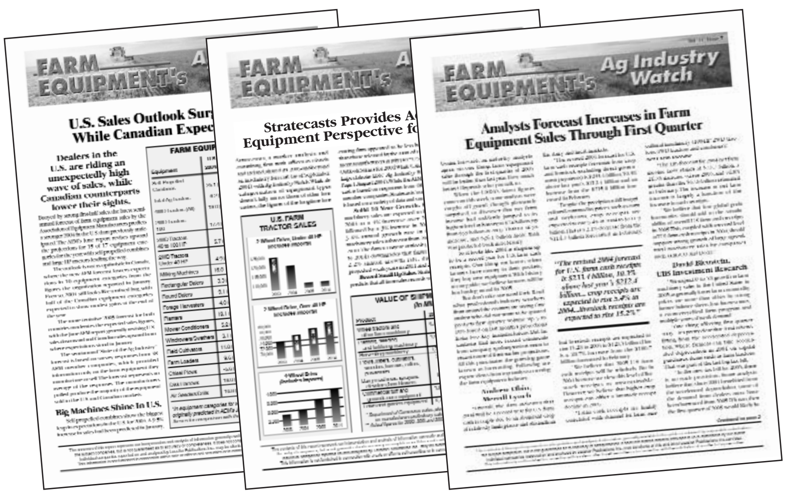


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