

Lifeline

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A Message From the CEO/General Manager Larry Peterson

The Heartland Board of Directors again this year spent a few days considering the future direction of the Cooperative at a Board planning conference. Because this year's main focus was to be on agronomy, St. Louis was chosen as the conference site. This allowed for time to be spent with our major seed partner, Monsanto.

This meeting sets the long term course for Heartland and is an important meeting for the Cooperative. From this direction, the stage is set for the actions of management and employees of Heartland. Because of the significance of the meeting, I felt it was important to give a brief update of the meeting proceedings.

The Board was asked to identify their greatest future concerns for the future of Heartland Co-op. The major concerns were:

- Direct purchases by farmers
- Competition
- Lack of trust/Losing trust
- Product logistics, especially in season
- Government's role; regulatory/compliance issues
- Supplier relationships
- Capital constraints
- Communications
- Sales effectiveness
- Farm consolidations

During the "Think Global" portion of the conference we touched on the overarching views of the agronomy and energy areas. We concentrated on three major areas in this segment.

- We spent time with key employees of Monsanto who set out the driving forces and challenges within their Company. The group took the opportunity to tour the Monsanto Chesterfield Research Center.
- Time was spent reviewing information from Mosaic and PCS, major fertilizer manufacturers, which summarized the current situation and their direction for the future. On hand was Annie Jones representing Terra Industries who developed the fundamentals of the current nitrogen fertilizer industry.
- A review of global drivers which are currently impacting the petroleum industry.

The remaining time was spent on the "Act Local" segment of the meeting. The specifics of marketing, sales and operational plans were shared by management staff. The Board reacted by agreeing with plans or suggesting modifications. Included was discussion on specific sales strategies, creating new service and product offerings, employee training, infrastructure development, risk management, environmental stewardship and operational plans.

The Board planning conference is an important event for developing the future direction of Heartland Co-op. It is used to communicate a direction that allows for understanding between the employee base

and the Board. With today's uncertainties and the volatility of commodity markets, setting a clear and logical course has never been more important.

SIX MONTH FINANCIAL REVIEW

December 31, 2008 ends the first half of Heartland's 2008-09 fiscal year. It is a good time to reflect upon the results of the Company as we head into the last half of the fiscal year. Up to this point, we are experiencing a very solid year in results. We are on track to surpass our year end budget expectations and prior year results.

In today's financial market unrest and credit upheaval, producing a solid bottom line is more important than ever.

These facts along with the volatility in the commodity markets have mandated that we provide an ample amount of working capital while maintaining an appropriate leverage position. As a cooperative bottom line profits are one of the only practical means of adding balance sheet strength. Therefore, having a substantial profit level is essential in the current marketplace.

There have been several factors that have led to our solid performance through the first six months of the fiscal year. Some of these factors will continue to positively impact our bottom line for the remainder of the year.

These factors include:

- Unwinding successful grain hedges established earlier
- Large drying income due to high moisture content of grain at harvest
- Grain arbitrage opportunities provided by latest mergers
- Late season chemical application
- Decreasing interest rates
- High propane usage for grain drying and unusually cold December
- Decreased fuel costs allowing for savings on vehicle fuel costs

Likewise, there remain many potential challenges to maintaining or increasing the bottom line by the June 30 fiscal year end. Some of the factors that are of concern and have already had an impact are:

- Uncertain economic times and credit crunch issues
- Onetime costs due to accessing adequate credit lines
- Unknown employee retirement funding needs
- Poor sales of fall fertilizer
- Reduced demand for fertilizer
- Grain quality issues based on crop maturity and moisture content

This year's results have the possibility of surpassing past records of bottom line performance. These results are not possible without the continued support of our customers. Thank you for your business during the first six months of the 2008-09 fiscal year. ■





Don't Look Back

Pricing our grain production is one of the toughest tasks we face in agriculture.

The degree of difficulty has increased several fold as we have moved to a more market oriented farm program. Like most task that we dislike or feel less than comfortable with, it is easy to ignore or put off until we have more time. Try as we might, common sense and logic seem to have little to do with figuring out the markets.

The conflict between hedging and speculating is as old as the first rocks that were traded. It is part of human nature and it will always take tremendous discipline to be an effective hedger. Hedging is not something you learn over night, in fact it is a constant learning experience. You must enjoy the challenge of learning, of winning and occasionally loosing. Hard as it is, we learn a lot more from loosing than we do from winning. The secret is the discipline to control our risk and minimize the losses. It is knowing that you will not always be right. That prices are not predictable but they are protectable.

The difficulty lies in the need to extract all we can from the market and at the same time protect the value and equity we have in the crop. Grain elevators and processors have achieved this task by hedging their purchases and looking to the futures market to pay their storage and carrying cost. Storage is on the income side of the financial statement rather than an expense. This same opportunity is available to farmers as well as others in the commodity business who must control their risk and protect the value they have in their production, factories and farms.

The hedger looks for above average futures prices to establish his hedges. Once that is accomplished, he turns to the futures spreads and basis to determine when the market needs the grain. If the market is not paying the storage and interest, the grain is moved to market. The hedging transaction is complete.

A major advantage of the hedger is that he is always looking forward. He is always looking for opportunities to maximize the return to his assets. The stress of trying to outguess the market and beating up on himself for being "wrong" is gone.

Farming is a wonderful occupation and the opportunities are endless. We need to find a way to enjoy this business and also keep it profitable.

The average price for new crop corn for January was \$4.35 and 9.71 for new crop soybeans. That gives us the perspective that these prices will be in the top 25% of the price range for the year. Anytime the market approaches our average price, we need to be ready to make sales.

Our current average price for corn from Jan 1 to Feb 18 is 4.25. For soybeans - it is 9.45. Dec 09 corn is at 3.95 at this writing and Nov 09 beans are 8.48. If I want to be on the top side of the market, this tells me I need to be patient until the market returns to the average and hopefully above the average. Thirty plus years of data tells me that it always has. I will take that risk.

One of my favorite baseball players was Satchel Paige. His famous quote was "Don't look back, they might be gaining on you" or something to that effect. Looking back in grain marketing is seldom a good thing to do but this is a classic and textbook year for the hedger. We must look back a bit to learn how much fun it can be. ■

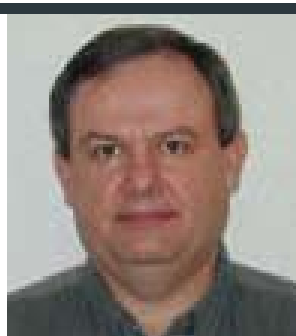
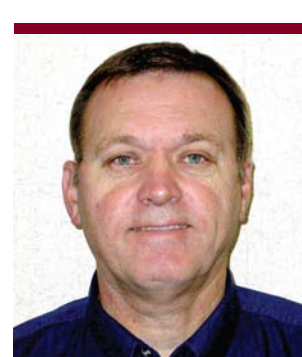
Beef Quality Assurance

Heartland, Heart of Iowa and the Iowa Beef Industry Council hosted a Beef Quality Assurance Certification on Wednesday February 18th at the Bill Couser Farm near Nevada. Thirty-five beef producers attended and Brian Waddingham from IBIC and Dr. Terry Engelkin from ISU led the training sessions.

Beef Quality Assurance is made possible in the state of Iowa with funding from the Iowa Beef Industry Council (IBIC) and the \$1 per head beef checkoff. Veterinarians, nutritionists, extension educators and other professionals from the Iowa

Veterinary Medical Association, Iowa State University, ICA and IBIC working with the program believe cattle produced and managed using BQA guidelines will be less likely to contain a violative residue, objectionable tissue damage and have more desirable uniform tenderness, juiciness and flavor.

Heartland is pleased to have the opportunity to partner with our Beef producers and Industry support Team to help ensure the quality and integrity of our meat supply and the security of the beef market. ■



Focus on Agronomy

Our agronomy focus is to utilize the latest technology to put

together the most profitable crop production plan for your operation. For the last 2 years we at Heartland Co-op have worked hard to make sure we can deliver on utilizing technology to improve our customer's profitability.

We have perfected the positioning of nutrients where they return the most dollars for your operation. We also match those nutrient recommendations with the right seed genetics and populations for your fields. Several of our customers have added equipment to their planters to eliminate overlapping and give them the ability to vary their seed population to fit the varied productivity levels of the soils.

Our precision ag department not only sold and installed the equipment but they also write the program to vary the seed population rates to fit those fields being planted. They can also set up your anhydrous toolbar to variably rate and apply the nitrogen to match up with the seed population changes in that field. We have come along way. Its hard to put a value on what this can bring to your operation. There are several benefits. By not having overlaps you save the input costs and you gain on yields. Pushing the production in the areas of the field that will respond gains you additional yields without adding more acres to your operation. Environmentally it is the right way to protect our environment and to utilize the nutrient investment.

We have perfected the positioning of nutrients where they return the most dollars for your operation.

If you have questions on putting this all together for your operation contact your agronomist.

When putting together your final plans for your production make sure you include ways to evaluate and learn how to improve profitability. There are several things you can look at without too much trouble. Hybrid and variety comparison are always a good thing. We encourage everyone to duplicate their comparisons to make sure the comparisons are accurate and not due to soil changes.

Populations are also something that can have a big impact. If you have comparisons you would like to make - we would welcome the opportunity to work with you. Give your agronomist a call for his input and suggestions for comparisons that you can work on together. ■



Petroleum News

delivery, we require all of our customers to honor theirs as well.

The petroleum market has become very volatile in the last few years.

CONTRACTING PROGRAMS

Refined Fuels & Propane

Heartland Co-op offers its customer refined fuels and propane programs to allow them to make choices. We offer a fixed price contract which allows you to lock in a price and we also offer a price at the time of delivery. This is the customer's choice to make. If the customer feels the price is going to be higher, they can lock in a fixed price and their price will not go up. Each customer must call us if they wish to contract. If they think the price is going to be lower, then they have the choice to not contract and pay the price we offer at the time of delivery.

The contracts we build with our suppliers are built upon the agreements and contracts signed just like the customers - with a fixed price. In order to honor our supplier contract commitment by taking

CRUDE OIL PRICING

1990's Average Price \$20
2003 Average Price \$31
2005 Average Price \$57
2006 Average Price \$66
June-08 Average \$134
October-08 Average \$77
December-08 Average \$43

Contracting is not always the right answer every year. No one knows which direction the market will go. Customers should use caution when contracting. Contact your local Heartland location to find out what refined fuel and propane contracts are available.

EQUIPMENT

Farm Fuel Tank Program

If you are a fuel customer of Heartland Co-op and you would like to add more diesel storage or just upgrade the tanks you have, now is the time.

- Program Ends: 5-01-09 or while supply lasts
 - 10 year payment program - or sale price is:
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THANK YOU FOR YOUR BUSINESS!

Outlook on Fertilizer

Fertilizer prices have been a primary topic of discussion through the winter months. The news media has written numerous commentaries and articles about the present situation that is presently pitting farmers against their local ag retailer in a standoff to see who is going to give first. It is my intent to use this forum to share some of the specifics of how we got into this dilemma, addressing the situation from Heartland's perspective, and project how we believe the markets may unfold this spring and summer. Our objective is to provide good information that allows you to make the best possible decisions for your farming operation.

Last spring, while the 2008 crop was being planted, ag retailers were challenged by fertilizer suppliers to make buying decisions for the 2009 crop year. World shortages of nitrogen, phosphorus, and potash were eminent, based on world demand, and if retailers didn't take a position on product, they faced the risk of not having product for customers for the fall 2008 and spring 2009 fertilizer seasons. Despite unprecedented high wholesale prices, Heartland, and many retailers throughout the country, took the risk of procuring product on your behalf. After all, we've always worked together based on trust and mutual understanding that we would have the product for you, at competitive prices, when you were ready to buy... often just a day or two before it was applied. This process has worked successfully for many years, and been profitable to both the farmer and the retailer.

All of this looked like a good decision until the sub-prime loan issues hit the economy, crude oil prices fell, and commodity prices followed. A world recession brought commerce to a halt, reversing some of the dynamics that had driven wholesale fertilizer prices to all-time highs. It should be noted, that despite some increase in retail fertilizer prices, ag retailers never followed wholesale prices upward at the same pace. In fact, during August 2008, there was a dramatic inversion between wholesale and retail pricing that was never noted by the media. Ag retailers were cognizant of grower input costs and recognized

farmers have a limit for how much they will pay for crop inputs in relation to market price. Demand destruction was occurring at these high levels. As a result of the shift in demand, the industry experienced a rapid free-fall of wholesale prices for urea and phosphorus. Other fertilizer products, such as potash and anhydrous ammonia, were not impacted as greatly due to a tighter supply / demand balance and logistical issues predicted for Spring 2009.

Current dilemma. Despite the rapid fall in wholesale prices, many ag retailers in Iowa have not dropped retail prices, respectively. This has created much concern from customers, and is generating various responses in the market. Some farmers are holding off purchasing, expecting prices to drop before spring. Some have explored alternative business models, by-passing the traditional channel. No one can say what is the best approach, but there are some pitfalls that should be noted.

It is not likely that retail prices will drop prior to the spring season. Heartland is monitoring retail pricing within our trade area, and positioned to sell at competitive levels against "like" retailers. "Like" retailers are those that have made millions of dollars in financial commitment in storage facilities, people, and equipment that have served your needs in a value-added manner during the past. Retailers are holding prices to protect this investment for long-term sustainability. If retailers cannot generate a return on their investment, moving to a lower cost structure means eliminating sales people and service/support infrastructure. Consider the value of these components as you make your crop nutrient decisions.

Those considering alternative market choices, such as purchasing their own applicator and trucking fertilizer from distant source points that may be offering lower prices, need to evaluate the expediency and efficiency of this business model. The economics look good, but what if complications develop? What if the truck lines at the terminals are extraordinarily long or the terminal equipment breaks down delaying application? What if your applicator breaks down early in the process? What if your operator is sick or changes jobs in the middle of the season? Do you have the size and scale to overcome these types of setbacks? How much will it cost a farmer in yield loss if we have a wet spring and planting is delayed beyond the optimal planting date?

If considering on-farm storage, be forewarned, stockpiling fertilizer on the ground is defined as a fertilizer spill subject to penalty by the Department of Ag. There are also consequences for environmental impairment if the product is mismanaged. These are all issues that ag retailers have encountered and are prepared to overcome in order to maintain the service levels you deserve.

Expect logistical issues. No matter what choices you make to fulfill your crop's nutrient needs, be aware that fall fertilizer applications were less than 1/2 of what normally gets applied. We expect unusually high demand for trucks and operators to address the demand surge that will come this spring. Lines at terminals are projected to be longer than normal, and product outages may occur after the initial inventories are depleted.

Make your plans now. Heartland has created a priority list for customers if/when we encounter logistic or product shortage issues. Those with prepaids and pre-planned orders will have priority over walk-in business.

What will happen to fertilizer prices after this spring? Again, nobody knows for certain, but there are a few signs that lead us to believe that retail prices for phosphorus and anhydrous ammonia may soften after the pre-plant season. Historically, NH3 prices drop for side-dress as retailers empty facilities and prepare for the next fall season. This could occur in 2009, depending on ending inventories.

Fertilizer prices will be re-calibrated as ag retailers complete their fiscal year-ends. General acceptable accounting practices require a business to re-value existing inventories to market price when they close their books. It is logical to assume that ag retailers will write-down over-valued inventories, and prices for next fall will reflect the lower wholesale costs in today's market. Hopefully, this will bring the existing stand-off between retailers and farmers back into balance. ■





2009 Construction Projects

The Heartland Co-op Board of Directors has approved the expansion and retrofit of three grain locations. The three projects include new storage and receiving capacity at Colo, new receiving and drying capacity at Elberon, and a new grain dryer at Waukee.

The Colo project will include a new 15,000 bushel per hour receiving system, a new 15,000 bushel per hour fill conveyor in the existing flat storage building, and a 500,000 bushel bin. This project is designed to allow for future facility expansion as needed to handle any future volume growth. The project layout will also allow for increased drying capacity at the location. The Elberon project will consist of an extensive remodeling of the grain receiving and handling systems. All of the fill conveyors will be replaced with 15,000 bushel per hour conveyors, a new 15,000 bushel per hour receiving pit and leg will be installed, and an additional 2400 bushel per hour grain dryer will be added. These changes will increase the functionality of the facility as well as allow for future grain volume, receiving, and storage capacity growth.

The Waukee project will include the replacement of the grain dryer which was lost during this past harvest season due to an extensive fire within the grain dryer. The project will included replacement of the grain dryer and installation of new wet and dry grain legs to match the increased capacity of the new drying system.

We invite you to stop by these locations to get further details of the projects and see the construction design prints. ■

Introducing our new Director of Grain Origination for the Western areas of Heartland Co-op's trade territory, Ron Groskreutz. Ron is an Illinois native that comes to us with over 20 years of experience in the grain industry. Ron has been a grain originator for a local coop, an Illinois River terminal Manager, and a Grain Department Manager in Wisconsin. He will have accountability for working with the membership and staff regarding marketing programs and grain market information. Ron can be reached at 515.974.4326 or 515.577.8043.



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