

Support for Farmers' Cooperatives

Final Report



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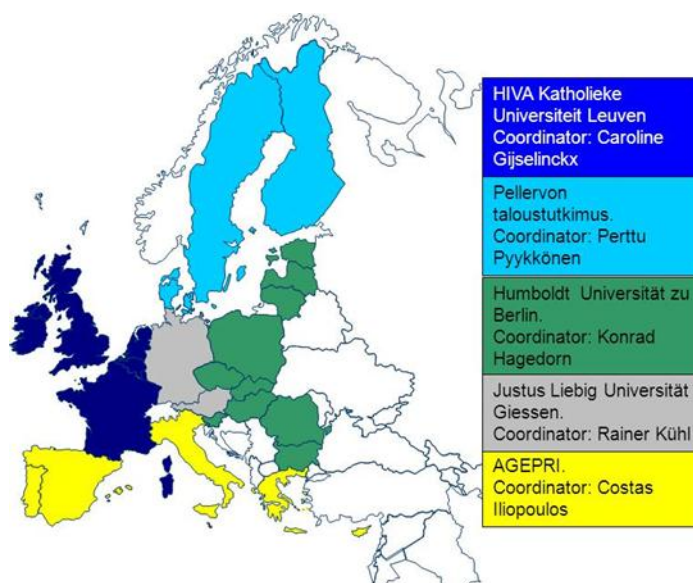
Preface and acknowledgements

In order to foster the competitiveness of the food supply chain, the European Commission is committed to promote and facilitate the restructuring and consolidation of the agricultural sector by encouraging the creation of voluntary agricultural producer organisations. To support the policy making process DG Agriculture and Rural Development has launched a large study, “Support for Farmers’ Cooperatives (SFC)”, that provides insights on successful cooperatives and producer organisations as well as on effective support measures for these organisations. These insights can be used by farmers themselves, in setting up and strengthening their collective organisation, and by the European Commission in its effort to encourage the creation of agricultural producer organisations in the EU.

This final report presents the main findings of the SFC project. It should be considered as a summary of the 77 reports that have been written within the framework of this project: 27 country reports, 8 sector reports, 6 EU-wide synthesis reports, 34 case studies, a report on a cluster analysis, and a study on the development of agricultural cooperatives in other OECD countries.

Although this final report has been edited by the first three authors mentioned on the cover, it is the result of the work of many others. We would like to thank all partners in the project for their effort and commitment: the five regional coordinators of the SFC project (see figure); the cooperative experts in the 27 EU Member States; the sector experts; the experts on legal affairs; the methodological experts that have guided this complex study; and finally the authors of the case studies. A list of all reports and authors can be found in Annex 1.

We would like to thank the interservice Steering Group of the European Commission, chaired by Mr. Tomas Garcia Azcarate (DG Agriculture and Rural Development) for its support. The study was tendered by a call for proposals and the discussions in the Steering Group were of high quality and always constructive. The scientific responsibility is ours.



We are most grateful for all those persons interviewed, in cooperatives, ministries, research institutes, associations that promote cooperatives, who gave us their valuable time and insights. Similar thanks go to the stakeholders that reacted to draft reports. We hope that at least some of our analysis is useful in their daily cooperative work.

Jos Bijman and Krijn J. Poppe
Project managers

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Executive Summary

Purpose and organisation of the study

The imbalances in bargaining power between the contracting parties in the food supply chain have drawn much scholarly attention but have also been closely examined by policy makers. The European Commission is committed to facilitate the restructuring of the agricultural sector by encouraging the creation of voluntary agricultural producer organisations. DG Agriculture and Rural Development has launched a large study, "Support for Farmers' Cooperatives" (hereafter: SFC), to provide background knowledge that will help farmers organise themselves in cooperatives as a means to consolidate their market orientation and so generate a solid market income. The specific objectives of the study are the following:

1. To provide a comprehensive description of the current level of development of cooperatives in the European Union. This description will pay special attention to the following drivers and constraints for the development of cooperatives:
 - a. Economic and fiscal incentives or disincentives and other public support measures at the regional and national levels;
 - b. Legal aspects, including those related to competition law and tax law;
 - c. Historical, cultural and sociologically relevant aspects;
 - d. The relationship between cooperatives and the other actors of the food chain;
 - e. Internal governance of the cooperatives.
2. To identify laws and regulations that enable or constrain cooperative development.
3. To identify specific support measures and initiatives which have proved to be effective and efficient for promoting cooperatives and other forms of producer organisations in the agricultural sector in the European Union.

This Executive Summary provides the main findings of the study. But before presenting these results, a brief description will be given of organization of the project, the theoretical framework used, and the research methods applied.

The study was carried out during 2011 and 2012, by a European research consortium consisting of the following institutes:

- LEI Wageningen UR, The Netherlands: Krijn J. Poppe
- Wageningen University, The Netherlands: Jos Bijman
- Pellervo Economic Research PTT, Finland: Perttu Pyykkönen
- University of Helsinki, Finland: Petri Ollila
- Agricultural Economics Research Institute, Greece: Constantine Iliopoulos
- Justus Liebig University Giessen, Germany: Rainer Kühl
- Humboldt University Berlin, Germany: Konrad Hagedorn, Markus Hanisch and Renate Judis
- HIVA Katholieke Universiteit Leuven, Belgium: Caroline Gijssels
- Rotterdam School of Management, Erasmus University, The Netherlands: George Hendrikse and Tony Hak

In addition to the work of these consortium members, important contributions were made by national cooperative experts in all of the 27 Member States of the EU (see Appendix 1 of the Final Report for the names of all national experts). The data gathered in all 27 Member States has been presented and analysed in individual country reports. The data collected was also used in preparing eight sector reports, focusing on the role of cooperatives in the following sectors: dairy, wine, fruit & vegetables, olives and olive oil, cereals, pig meat, sugar and sheep meat. In addition, cross-cutting themes were studied at the EU level, leading to six EU synthesis and comparative analysis reports on the following themes: internal governance; policy measures; position in the food chain; social, historical and cultural aspects; legal aspects; and transnational cooperatives.

In the second phase of the project, 33 cases studies have been carried out, and the situation in selected non-EU OECD countries has been investigated. The 33 case studies were divided into 15 transnational case studies and 18 national or sector case studies. Some of the case studies focused on individual cooperatives, others studied all cooperatives in a particular country or sector.

All of these background reports on the state of development in countries and sectors, these case studies, the EU-wide analyses, and the overview of experiences in other OECD countries, provide farmers, cooperatives and policy makers with useful insights regarding the market position and organisation of cooperatives and producer organisations as well as on the potential supporting and restraining role different regulations and policy measures may have on the development of those cooperatives and producer organisations.

Theoretical framework

The starting point of this study is the assumption that there are at least three main factors that determine the success of cooperatives in food chains. These factors relate to (a) position in the food supply chain, (b) internal governance, and (c) the institutional environment. These three factors constitute the three building blocks of the analytical framework adopted in this study in order to explain the performance of cooperatives (Figure A).

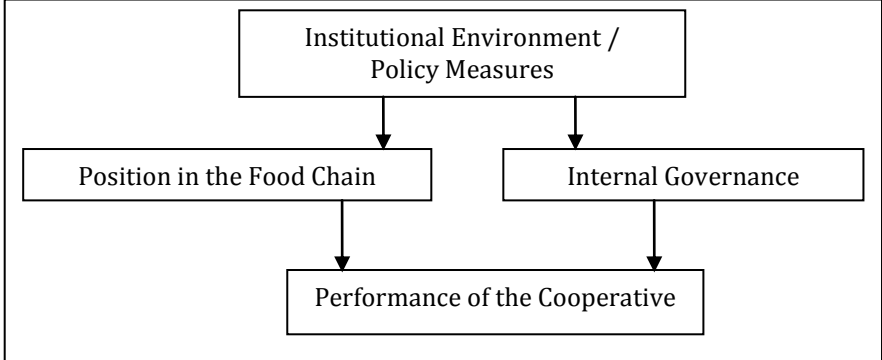


Figure A. The core concepts of the study and their interrelatedness

The position of cooperatives in the food supply chain refers to the competitiveness of cooperatives vis-à-vis its partners, such as processors, wholesalers and retailers. It also refers to the strategy that the cooperative follows in choosing a particular position in the food chain. Internal governance refers to the decision-making processes adopted, the role of the different governing bodies, and the allocation of control rights to members and professional management. Further, the internal governance refers to issues such as the organisational structure of the cooperative enterprise (e.g. the formation of holding and daughter companies). The institutional environment refers to the social, cultural, political and legal context in which cooperative operates, and which may have a supporting or constraining effect on the cooperatives' performance. History is an important ingredient of the institutional environment. For example, positive past experiences of cooperative development usually have resulted in the generation of trust and has boosted social capital – both necessary for efficient operation of the cooperative as well as for establishing new cooperatives. Legal aspects of the institutional environment, such as taxation and competition laws, are equally crucial in fostering or deterring cooperative development.

In defining cooperatives and producer organisations we have applied the three basic principles developed by Dunn (1988):

1. The User-Owner Principle: Those who own and finance the cooperative are those who use the cooperative.
2. The User-Control Principle: Those who control the cooperative are those who use the cooperative.
3. The User-Benefits Principle: The cooperative's sole purpose is to provide and distribute benefits to its users on the basis of their use.

These are simple and flexible principles, still encompassing a latitude of practices such as open or defined membership and one-member-one-vote or proportional voting. These basic cooperative principles can be found in the following organisational practices. Users typically control cooperatives by democratic decision-making structures. Capitalization of cooperatives is created by direct investments, retained patronage refunds, and per-unit capital retains. Benefits are realized by returning net income (or surplus) to patrons in proportion to use, by receiving/paying fair prices, and by gaining access to markets, supplies, and services. In sum, a cooperative has been defined as a "user-owned and controlled business from which benefits are derived and distributed on the basis of use" (Dunn, 1988: 85). While many different types of agricultural cooperatives exist in the EU Member States, our study focused on marketing cooperatives.

Main findings

Farmers' cooperatives play an important role in helping farmers to capture a higher share of the value added in the food supply chain in all Member States. The key functions of all marketing cooperatives are improving the bargaining power of their members and letting members benefit from economies of scale. In addition, cooperatives are reducing market risks, reducing transaction costs, providing access to resources, and strengthening their competitive position through product innovation and guaranteeing food quality and safety. A large number of cooperatives have expanded their activities in downstream stages of the food chain, thus strengthening their customer and consumer orientation by enhancing efforts in marketing (including branding), product innovation, and customization.

As agrifood supply chains are generally characterised by bargaining imbalances between farmers and their upstream and downstream partners, cooperatives play a key role in strengthening bargaining power and thus maximizing their members' share of the value added. However, generally the countervailing power of cooperatives vis-à-vis their retail customers is limited. The need for further strengthening bargaining power will most likely lead to more (international) mergers among cooperatives, while such mergers are also induced by seeking economies of scope in R&D and branding. To support farmers in this trend, legal definitions of producer organisations and support measures should not discriminate against large cooperatives. As this (international) growth process is often accompanied by changes in the internal governance, it holds the risk of a loss of member control over the cooperative firm.

We found that a large market share for cooperatives in a particular sector and country can increase the price level and reduce the price volatility, as is currently the case in the dairy sector. Also non-member farmers in this sector and country benefit from the large market share of the cooperatives. These non-member farmers may even benefit more, as IOF competitors generally pay higher prices. These findings are in line with the competitive yardstick theory. Cooperatives also continue to be important for reducing market risks for farmers, notably the risk of receiving payment for the deliveries.

A special type of farmers' cooperative is the bargaining association. Bargaining associations promote farmers' interests and are also a valuable partner for food processors, wholesalers and retailers, as they coordinate the supply of large volumes of products of homogeneous quality. Unlike marketing cooperatives, bargaining associations do not own assets and, usually, do not assume ownership of their members' produce at any stage of production or marketing. These associations are mainly active in the dairy and fruit & vegetable sectors. In Germany, they are also active in selling cattle and pigs.

A number of cooperatives and producer organisations perceive legal uncertainty in competition law and report high legal costs. They see a lack of coherence between the agricultural policy that promotes bundling under the Common Market Organisation (CMO), and competition policy that seems to prohibit information sharing and other forms of collaboration. Some other OECD countries (e.g. USA) have more – albeit under strict conditions – exemptions for cooperatives in competition law to rebalance market power.

Farmers have multiple options in organising the internal governance of their cooperative. In many cooperatives, however, there is room for strengthening management and supervision capacities. Most national laws provide sufficient flexibility for cooperatives to choose an internal governance model that fits the strategy of the cooperative, although such flexibility may not always be accompanied with – the so much needed – guidance. In some countries cooperatives and national legislators need to pay more attention to the ability of farmer-members to effectively control both the board of directors and the professional management, for instance by strengthening the capacities of the supervisory board and by allowing non-member experts in boards of directors and supervisory boards.

More than 300 European, national and regional policy measures were identified. Cooperative legislation, competition rules, and financial inducements were among those observed most often. There exist considerable differences between Member States, in terms of policy measures adopted. There are no clearly established links between the (current) support measures for farmers' cooperatives and the market share of these organisations. Also in other OECD countries it is hard to find an unambiguous link between legislation and cooperative performance.

Many support measures could potentially benefit cooperatives. Cooperatives particularly benefit from a flexible cooperative law, single taxation, and clearly defined competition rules. In some sectors producer organisations and cooperatives have benefitted from the CAP and some of its reforms (such as in the wine and F&V industries). We recommend that governments at the national and EU levels develop policies and measures to support capacity building and technical (organisational) assistance, especially in for small and start-up cooperatives. This is particularly true for the New Member States, where self-organisation is hampered by a lack of social and human capital.

The links between cooperatives and rural development are manifold. Cooperatives are often important employers and contributors to the regional economy. They contribute to public policy objectives such as the development of human capital, the improvement of competitiveness, and environmental sustainability. Quite a number of cooperatives build their strategy on regional characteristics, like in developing and marketing regional specialties.

Additional findings

All Member States have a cooperative tradition, although its origin and intensity differs. In some countries, the cooperatives are directly linked to market failure in large agricultural transitions at the end of the 19th century (Denmark, the Netherlands), or a movement for independence (Finland), others have seen periods where cooperatives were not politically correct (Portugal), or where the cooperative was not based anymore on self-organisation principles but was used as a

socialist planning tool instead (New Member States). Consequently, the label “cooperative” has different connotations in different regions.

The marginal role played by cooperatives in some countries (and especially in the New Member States) has an important social background: the low level of self-organisation and networking is not only a barrier to cooperative development but represents a persisting societal characteristic with far broader implications.

Cooperatives account for a large share of farm product market in some sectors but not in others. Figure B shows the EU average; substantial differences exist, however, per country. The differences among the sectors are mainly due to the characteristics of the product and the production process. In the dairy and fruit & vegetables sectors cooperatives have an important market share due to the perishability of the product and thus the high transaction costs in trading this product. Also in wine and olive oil, cooperatives have a substantial although sometimes minority market share. In sectors like cattle, pigs and sheep, the animals are often sold under contracts to traders or non-cooperative slaughterhouses, but in some countries cooperatives continue to have substantial market shares in these sectors.

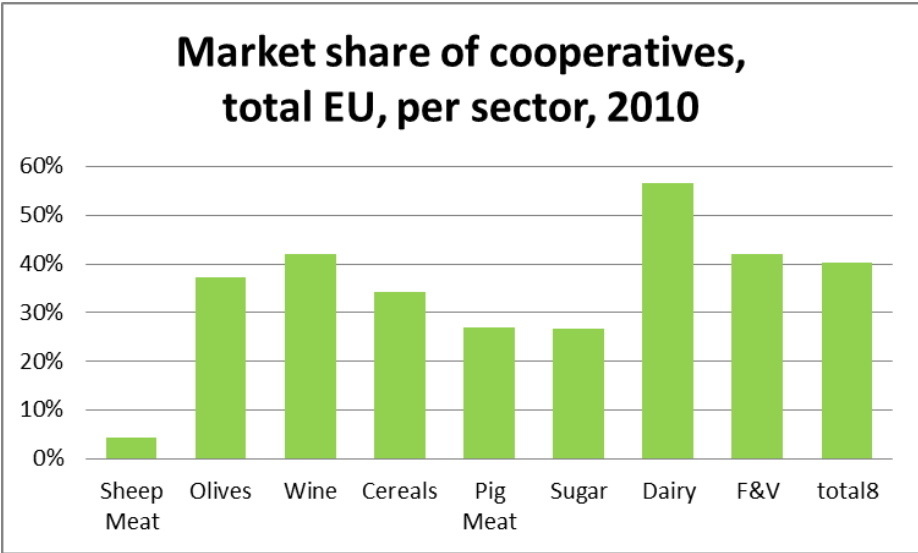


Figure B. Market share of cooperatives per sector, for EU as a whole.

Professional structures and policies regarding board composition and member participation affect the performance of cooperatives. Proportional voting rights, professional management, supervision by outsiders, and selection of directors on the basis of expertise or product representation and not regional origin, all have a positive effect on cooperative performance.

Branding activities performed by cooperatives differ by sector. Branded consumer products can be found in the dairy and wine sectors and, to a lesser extent, in the fruit & vegetables and olive oil sectors. They are, however, rare in the cereals, sugar, sheep and pig meat sectors.

Federated cooperatives are important in sectors and regions with many small cooperatives. They can obtain the economies of scale and bargaining power that local cooperatives cannot. However, as the long-run trend is that primary cooperatives become larger and more directly involved in marketing their products, the federated cooperative model may in the end disappear.

Several cooperatives have evolved into hybrid forms. This hybridization refers both to adopting organisational structures similar to those of investor-owned firms (IOFs) and to the development of non-user ownership structures. Cooperatives with hybrid ownership structures

are still majority-owned by farmers, but not necessarily by farmers as users of the services of the cooperative but as members of a farmers' organisation. In these cases, one or more farmer organisations are among the owners of the cooperative. In addition, cooperatives with hybrid ownership structure may have allocated ownership rights to investors from outside the agricultural sector.

In addition there are many producer organisations that follow cooperative principles in their structure and operations but are not cooperatives as defined by national cooperative legislation. Whether farmers choose the cooperative (legal) form to strengthen their market position and bargaining power is usually driven by practical and not by ideological arguments, and depends very much on the institutional context, including legal, social and cultural aspects.

We found 46 transnational cooperatives (i.e., cooperatives with members in more than one Member State). They can be found mainly in the dairy and fruit & vegetables sectors in northwest Europe. They often have foreign subsidiaries that source from non-member suppliers, like the 45 international cooperatives that we also found. Most cooperatives prefer to internationalise by acquiring or setting up foreign IOFs, and not by merging with other cooperatives or inviting foreign farmers to become members. Avoiding the dilution of ownership (income and control rights) is cited as the main reason for this development. There are no dissuasive legal barriers in merging across borders.

The situation in the New Member States is diverse and contrasting due to differences in historical backgrounds, pre-collectivisation land reforms, post-collectivisation transformation laws, cooperative traditions and collective memories, policy streams and social and cultural contexts. However, all cases have in common that the impact of the communist legacy persists, as low trust is an obstacle to cooperative development. Building trust and coping with free rider problems, often in poor regions with vulnerable rural communities, reflect pioneer activities that resemble early stages of the cooperative movement in Western Europe. This calls for trustworthy and skilful leaderships.

The capitalisation of cooperatives is a major constraint in some regions, where risk capital and other forms of equity are not readily available or cooperatives fail to provide their members with adequate incentives. However, capitalisation is not the only or even the main barrier to cooperative development and often the (lack of a profitable) business model is a much more binding constraint.

Synthetic summary

Background

Given the imbalances in bargaining power between contracting parties along the food supply chain, the European Commission (DG Agriculture and Rural Development) has launched a large study to gain better insights in the policies that could help farmers to self-organise in cooperatives as a means of strengthening their market position and so generating a solid market income. The specific objectives of this study were 1) to provide a comprehensive description of the current level of development of cooperatives in the EU, 2) to identify laws and regulations that enable or constrain cooperative development, and 3) to identify specific support measures, which have proved to be effective and efficient in promoting cooperatives and, more generally, producer organisations.

This report provides the overall conclusions of the full study. It was carried out by a European research consortium during 2011 and 2012. Data gathered in all 27 Member States has been presented and analysed in separate country reports. The data collected were also used in preparing eight sector reports, focusing on the role of cooperatives in each of these sectors. At the EU level a number of analyses were performed, studying aspects such as the institutional environment, internal governance, and the position of cooperatives in food supply chains. In addition, 34 cases studies have been carried out, and the situation in selected non-EU, OECD countries has been investigated. These background reports on countries, sectors and cases, as well as the EU-wide analysis, provide farmers, cooperatives and policy makers with useful insights regarding the market orientation and organisation of cooperatives and producer organisations.

Main findings

Farmers' cooperatives play an important role in helping farmers to capture a higher share of the value added in the food supply chain in all Member States. The key functions of all marketing cooperatives are improving the bargaining power of their members and letting members benefit from economies of scale. In addition, cooperatives are reducing market risks, reducing transaction costs, providing access to resources, and strengthening their competitive position through product innovation and guaranteeing food quality and safety. A large number of cooperatives have expanded their activities in downstream stages of the food chain, thus strengthening their customer and consumer orientation.

As most chains are characterised by bargaining imbalances between farmers and their upstream and downstream partners, cooperatives play a key role in strengthening bargaining power. However, generally the countervailing power of cooperatives vis-à-vis their retail customers is limited. The need for further strengthening bargaining power will most likely lead to more (international) mergers among cooperatives, while such mergers are also induced by the need to gain economies of scope in R&D and branding. To support farmers in this trend, legal definitions of producer organisations and support measures should not discriminate against large cooperatives. As this (international) growth process is often accompanied by changes in the internal governance, it holds the risk of a loss of member control over the cooperative firm.

We found that a large market share for cooperatives in a particular sector and country can increase the price level and reduce the price volatility, as is currently the case in the dairy sector. Also other farmers in this sector benefit from the large market share of the cooperatives. These non-member farmers may even benefit more, as IOF competitors generally pay higher prices. These findings are in line with the competitive yardstick theory. Cooperatives also continue to

be important for reducing market risks for farmers, notably the risk of receiving payment for the deliveries.

Bargaining associations promote farmers' interests and are also a valuable partner for food processors, wholesalers and retailers, as they coordinate the supply of large volumes of products of homogeneous quality. Unlike marketing cooperatives, bargaining associations do not own assets and, usually, do not assume ownership of their members' produce at any stage of production or marketing. These associations are mainly active in the dairy and fruit & vegetable sectors. In Germany, they are also active in selling cattle and pigs.

A number of cooperatives and producer organisations perceive legal uncertainty in competition law and report high legal costs. They see a lack of coherence between the agricultural policy that promotes bundling under the Common Market Organisation (CMO), and competition policy that seems to prohibit information sharing and other forms of collaboration. Some other OECD countries (e.g. USA) have more – albeit under strict conditions – exemptions for cooperatives in competition law to rebalance market power.

Farmers have multiple options in organising the internal governance of their cooperative. In many cooperatives, however, there is room for strengthening management and supervision capacities. Most national laws provide sufficient flexibility for cooperatives to choose an internal governance model that fits the strategy of the cooperative, although such flexibility may not always be accompanied with – the so much needed – guidance. In some countries there is a need to pay attention to the ability of farmer-members to effectively control both the board of directors and the professional management, e.g., by strengthening the capacities of the supervisory board and by having also outside experts participating in boards of directors and supervisory boards.

More than 300 European, national and regional policy measures were identified. Cooperative legislation, competition rules, and financial inducements were among those observed most often. There exist considerable differences between Member States, in terms of policy measures adopted. There are no clearly established links between the (current) support measures for farmers' cooperatives and the market share of these organisations. Also in other OECD countries it is hard to find an unambiguous link between legislation and cooperative performance.

Many support measures could potentially benefit cooperatives. Cooperatives particularly benefit from a flexible cooperative law, single taxation, and clearly defined competition rules. In some sectors producer organisations and cooperatives have benefitted from the CAP and some of its reforms (such as in the wine and F&V industries). We recommend that governments at the national and EU levels develop policies and measures to support capacity building and technical (organisational) assistance, especially in for small and start-up cooperatives. This is particularly true for the New Member States, where self-organisation is hampered by a lack of social and human capital.

The links between cooperatives and rural development are manifold. Cooperatives are often important employers and contributors to the regional economy. They contribute to public policy objectives such as the development of human capital, the improvement of competitiveness, and environmental sustainability. Quite a number of cooperatives build their strategy on regional characteristics, like in developing and marketing regional specialties.

Additional findings

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(Finland), others have seen periods where cooperatives were not politically correct (Portugal), or where the cooperative was not based anymore on self-organisation principles but was used as a socialist planning tool instead (New Member States). Consequently, the label “cooperative” has different connotations in different regions.

The marginal role played by cooperatives in some countries (and especially in the New Member States) has an important social background: the low level of self-organisation and networking is not only a barrier to cooperative development but represents a persisting societal characteristic with far broader implications.

Professional structures and policies regarding board composition and member participation affect the performance of cooperatives. Proportional voting rights, professional management, supervision by outsiders, and selection of directors on the basis of expertise or product representation and not regional origin, all have a positive effect on cooperative performance.

Several cooperatives have evolved into hybrid forms. This hybridization refers both to adopting organisational structures similar to those of investor-owned firms (IOFs) and to the development of non-user ownership structures. Cooperatives with hybrid ownership structures are still majority-owned by farmers, but not necessarily by farmers as users of the services of the cooperative but as members of a farmers’ organisation. In these cases, one or more farmer organisations are among the owners of the cooperative. In addition, cooperatives with hybrid ownership structure may have allocated ownership rights to investors from outside the agricultural sector.

In addition there are many producer organisations that follow cooperative principles in their structure and operations but are not cooperatives as defined by national cooperative legislation. Whether farmers choose the cooperative (legal) form to strengthen their market position and bargaining power is usually driven by practical and not by ideological arguments, and depends very much on the institutional context, including legal, social and cultural aspects.

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The situation in the New Member States is diverse and contrasting due to differences in historical backgrounds, pre-collectivisation land reforms, post-collectivisation transformation laws, cooperative traditions and collective memories, policy streams and social and cultural contexts. However, all cases have in common that the impact of the communist legacy persists, as low trust is an obstacle to cooperative development. Building trust and coping with free rider problems, often in poor regions with vulnerable rural communities, reflect pioneer activities that resemble early stages of the cooperative movement in Western Europe. This calls for trustworthy and skilful leaderships.

1 Introduction

1.1 Objective of the study

The imbalances in bargaining power between the contracting parties in the food supply chain have drawn much scholarly attention but have also been closely examined by policy makers. The European Commission is committed to facilitate the restructuring of the sector by encouraging the creation of voluntary agricultural producer organisations. DG Agriculture and Rural Development has launched a large study, “Support for Farmers' Cooperatives” (hereafter: SFC), that provides background knowledge that will help farmers organise themselves in cooperatives as a means of consolidate their market orientation and so generate a solid market income. This report provides the overall conclusions of the full study (for more details and much of the evidence of our findings, we refer to the 77 underlying background reports that are listed in Annex 1).

Under the assignment from the European Commission, the specific objectives of the study are the following:

First, to provide a comprehensive description of the current level of development of cooperatives in the European Union. This description will pay special attention to the following drivers and constraints for the development of cooperatives:

- Economic and fiscal incentives or disincentives and other public support measures at the regional and national levels;
- Legal aspects, including those related to competition law and tax law;
- Historical, cultural and sociologically relevant aspects;
- The relationship between cooperatives and the other actors of the food chain;
- Internal governance of the cooperatives.

Second, to identify laws and regulations that enable or constrain cooperative development and third, to identify specific support measures and initiatives which have proved to be effective and efficient for promoting cooperatives and other forms of producer organisations in the agricultural sector in the European Union.

1.2 Analytical framework

The starting point of this study is the assumption that there are at least three main factors that determine the success of cooperatives in food chains. These factors relate to (a) position in the food supply chain, (b) internal governance, and (c) the institutional environment. The position of cooperatives in the food supply chain refers to the competitiveness of cooperatives vis-à-vis its partners, such as processors, wholesalers and retailers. This term encourages sector- and product-specific aspects that have a significant impact on the clauses of the contractual agreements between the various food supply chain participants, as well as relevant public policies. Further, the competitive position of cooperatives in food supply chains influences and is influenced by the structure of agriculture and the organisation of the food industry. A crucial determinant of cooperatives' competitive position is the type of strategy they pursue.

Internal governance refers to the decision-making processes adopted, the role of the different governing bodies, and the allocation of control rights to members and professional management (and the associated agency problems). Further, internal governance refers to the organisational structure of the cooperative enterprise (e.g. the formation of holding and daughter companies).

The institutional environment refers to the social, cultural, political and legal context in which cooperatives operate, and which may have a supporting or constraining effect on the

cooperatives' performance. History is an important ingredient of the institutional environment. For example, positive past experiences of cooperative development usually result in the generation of trust and boosts social capital – both necessary for efficient operation of the cooperative and in forming new cooperatives. Legal aspects of the institutional environment, such as taxation and competition laws, are equally crucial in fostering or deterring cooperative development.

The three factors constitute the three building blocks of the analytical framework adopted in this study in order to explain the performance of cooperatives (Figure 1.1).

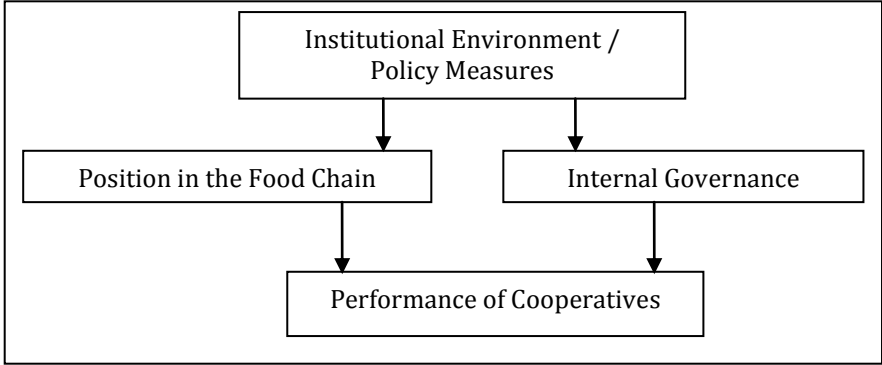


Figure 1.1. The core concepts of the study and their interrelatedness

Cooperatives may, and usually do, distribute all surplus (income from transactions with members) and profits (income from transactions with non-members) to current members, after deducting operating expenses. Therefore, using profits as an indicator of performance is not available to cooperatives. Cooperatives and Investor-Owned Firms (IOFs)¹ pursue different objectives and thus comparing their performance is extremely difficult or impossible². Throughout this study we mainly use the market share of cooperatives³ and its evolution as a proxy for cooperative performance; a higher and increasing market share indicates an efficient performance. The differences in the objectives pursued by cooperatives and IOFs are exemplified in the common case where a food processing IOF exits a market or an industry when return on investment falls under the level demanded by the investor-owners of the firm. Subsequently, local farmers form a processing cooperative that absorbs members' produce and generates a bundle of benefits for members and the local communities.

It would be ideal to measure performance using prices paid to farmers. That however is tricky. First of all due to the lack of relevant data (and products for which these prices are compared should be standardised in a lot of aspects). Second because the Competitive Yardstick Theory suggests that if cooperatives are price-setters in a region, IOFs have to pay higher prices, too. We have been able to test this theory in the dairy market (see Chapter 6). Member satisfaction is also a proxy of a cooperative's performance, particularly if it is compared to the satisfaction of farmers delivering to IOFs. Such data, however, were not available for this study. It was not possible in this study to gather data on stated member satisfaction (and compare it to satisfaction of farmers delivering to an IOF).

¹ It is nowadays common in (economic) literature on cooperatives to compare the cooperative to an Investor-Owned Firm (IOF), where the IOF essentially represents any non-cooperative firm.

² See, for instance, Soboh et al. (2012) who show that part of the observed divergences in the performance of cooperatives and IOFs is due to their different objectives.

³ Where market share in this report is the combined market shares of all cooperatives in a sector compared to the cumulative market share of all IOFs in the same sector, both measured at farm-gate transaction.

1.3 Definition of the cooperative

In this SFC study we follow what Dunn (1988: 85) has called the basic cooperative principles. The three principles are:

1. The User-Owner Principle: Those who own and finance the cooperative are those who use the cooperative.
2. The User-Control Principle: Those who control the cooperative are those who use the cooperative.
3. The User-Benefits Principle: The cooperative's sole purpose is to provide and distribute benefits to its users on the basis of their use.

These are simple and flexible principles, still encompassing a latitude of practices such as open or defined membership and one vote per member or proportional voting. These basic cooperative principles can be found in the following organisational practices. Users typically control cooperatives by one-member-one-vote, but voting may be proportional to patronage, equity investment or a combination of patronage and equity investment. Capitalization of cooperatives is created by direct investments, retained patronage refunds, and per-unit capital retains. Benefits are realized by returning net income (or surplus) to patrons in proportion to use, by enjoying prices, and by gaining access to market, supplies, and services. In sum, a cooperative can be defined as a "user-owned and controlled business from which benefits are derived and distributed on the basis of use" (Dunn, 1988: 85).

Agricultural cooperatives exist in many different kinds and types. On the basis of a literature review of the classifications and typologies of farmer-owned cooperatives, we selected the following seven classifications that have been used throughout the SFC study. A cooperative can be classified on the basis of:

1. the sector(s) in which it operates or the main product it is handling (e.g. dairy, cereals, wine, pig meat, etc.);
2. the main functions it performs, such as joint production, providing farm inputs, processing farm products, marketing farm products, etc.;
3. the diversity of functions and products it covers, such as focussing on economic activities (for one or multiple products), or also including social and political activities;
4. the position it has in the food chain (or the extent of vertical integration), ranging from only collecting farm products to selling branded products directly to consumers;
5. the type of members it has, distinguishing between primary (or first-tier) cooperatives that have farmers as members and federated (or second-tier) cooperatives that have primary cooperatives as their members;
6. the geographical scope of the membership; ranging from local, regional, national to international and transnational; An international cooperative is defined as a cooperative that sources from non-member farmers in other countries. A transnational cooperative, on the other hand, has members in several countries.
7. the financial/ownership structure; ranging from traditional cooperatives, proportional investment cooperatives, member-investor cooperatives, new generation cooperatives, cooperatives with capital seeking entities, to investor shared cooperatives (Nilsson, 1999; Chaddad and Cook, 2004).

Cooperative or Producer Organisation?

Producer Organisations (POs) are economic organisations of agricultural producers (or fishermen) with characteristics similar to those of cooperatives. The concept of PO is well-known in the literature on developing countries (e.g., Rondot, 2001; World Bank, 2007) as well as on transition countries (e.g., Gardner and Lermann, 2006; Banaszak, 2008). A PO may have the legal form of a cooperative, but in many cases it has not, either because the legal requirements for cooperatives pose many restrictions on the activities and the structure of the

PO, or, as in countries that have transformed from a socialist state economy, because the term cooperative has a negative connotation. For instance in Poland, the majority of producer groups (a term used in Polish legislation on promoting farmer-controlled collective marketing) have the legal form of a limited liability company; only 30% of the producer groups are registered as cooperatives (Matczak, 2011).

Another practical distinction between a cooperative and a PO is that the latter usually has a more focussed objective; mainly the joint selling of members' products. Also, a PO is usually positioned at the upstream part of the food chain. Thus, a PO is often involved in joint bargaining with customers, and much less with processing of members' products. A common definition of a PO is the following: a producer organisation is a rural business, owned and controlled by producers, and engaged in collective marketing activities (Penrose-Buckley, 2007). Thus, in a broad sense, POs are, like cooperatives, user-owned, user-controlled, and user-benefit organisations.

Producer associations in Germany

In various sectors of German agriculture a specific type of producer organisation exists that is similar but not identical to a cooperative. This is the so-called producer association (Erzeugergemeinschaft, or EZG), whose main function is collective bargaining. These EZGs are founded in accordance with the 1968 German Law on Market Structures (Marktstrukturgesetz). This law allows exceptions from the application of German national competition law in the agricultural sector in those cases where horizontal collaboration among farmers and vertical collaboration between the EZG and processors will lead to the supply and marketing of agricultural products being better tailored to market requirements. EZGs not only organise joint sales and transport of agricultural products but also set up rules that improve the quality and homogeneity of farm products. They typically have close relationships with member-farmers and oblige them to market all their products through the EZG. From a business organisation law perspective, EZGs are not organised as cooperatives but registered as for-profit associations. Nevertheless, as their main objectives and decision-making structure are similar to those of the cooperative, EZGs can be regarded as a special form of marketing cooperatives.

POs in EU legislation

The term Producer Organisation has become well-known in the European Fruit and Vegetables (F&V) industry since the Common Market Organisation (CMO) for Fruit & Vegetables was introduced in 1996.⁴ Under this CMO for F&V a recognised PO is defined as an organisation formed on the initiative of farmers who are growers of particular F&V, and which has one of the following objectives (i) ensuring that production is planned and adjusted to demand, particularly in terms of quality and quantity; (ii) concentration of supply and the placing on the market of the products produced by its members; (iii) optimising production costs and stabilising producer prices.⁵ Recognised POs are eligible for EU financial support. Because a PO is obliged to apply rules that enable producer members to democratically monitor and control their organisation and its decisions, it is rather similar to a cooperative. However, the EU legislation explicitly states that a PO can adopt any legal entity or can be clearly defined as part of a legal entity. Thus, other organisations than cooperatives are also recognised as POs. In many EU Member States, however, POs have adopted the legal business form of a cooperative.

As of 2007, the concept of recognised Producer Organisation, being an organisation of farmers that supports the marketing of their products, has been broadened to the hops, olive oil

⁴ Regulations (EC) No 2200/96, No 2201/96 and No 2202/96, respectively for fresh fruit and vegetables, processed fruit and vegetables and citrus intended for processing were adopted in October 1996. Already in 1972, POs were defined in EU legislation as any organization of fruit and vegetable producers which is established on the producers' own initiative for purposes such as promoting concentration of supply and the regularization of prices at the producer stage of the food chain and making suitable technical means available to producer members for presenting and marketing the relevant products (Regulation (EC) No 1035/1972).

⁵ Council Regulation (EC) No 1182/2007, which laid down the reform of the 1996 Regulations.

and table olives, and silkworm sectors.⁶ Besides the requirement of being established by producers of one of the mentioned products, the only requirements for recognised POs are related to their function: recognised POs should pursue specific aims related to (i) concentrating supply and marketing the produce of the members; (ii) adapting production jointly to the requirements of the market and improving the product; (iii) promoting the rationalisation and mechanisation of production. No further requirements as to ownership or decision-making procedures apply.

In March 2012, the concept of PO has also been introduced in the EU legislation on the European dairy market.⁷ In order to reinforce the bargaining power of milk producers, farmers can join together in POs that can negotiate collectively the contract terms including the price of raw milk. Again, no specific requirements as to democratic decision-making or farmer-ownership apply.

The SFC project has focussed as much as possible on cooperatives. Where POs are very similar to cooperatives, they have been included in the study. The term cooperative is used as a shorthand for cooperatives and producer organisations (unless they are explicitly mentioned separately).

Ambiguous cases: hybrids

Although the definition of a cooperative being user-owned, user-controlled, and for user-benefit seems clear, in practice there are ambiguous cases. We identified a number of enterprises that seem to work in the spirit of a cooperative, but are owned by farmers' organisations (like the slaughterhouse VION owned by the Dutch farmer organisation ZLTO). In some cases, a cooperative owns an IOF in a different sector or country, and there are limited companies that insist they are not cooperatives but where most of the shares are held by farmers (e.g., HZPC in the Netherlands) or where the situation is unclear (like NordZucker in Germany that is owned by regional companies with many, and perhaps mostly, farmers as owners). We studied some of these cases in more detail (see Chapter 5).

1.4 Literature

The SFC project's methodology (see Chapter 2) is grounded in the scientific literature on agricultural cooperatives. A thorough evaluation of the assumptions and findings presented in the literature has been carried out and used to define research questions and hypotheses in the project. An overview of the reviewed literature has been delivered to the European Commission in the form of an Endnote database.

Seen the purpose of this final report (to report our findings on the state of affairs in European cooperatives and the support measures for them) it is out of the scope to summarise the scientific literature in detail. Where useful we will refer to it in our analysis in the next chapters (and more can be found in the reports listed in Annex 1).

Table 1.1. provides a summary of themes investigated in the literature, taken from Hendrikse & Feng (2012). Some of these themes provide explanations for the existence of cooperatives; others discuss challenges or problematic aspects of the cooperative form in doing business.⁸

1.5 Period under study

This report covers the period from 2000 to 2010 and presents the most up-to-date information available. This refers to both the factual data that has been collected and the literature that has been reviewed. Where appropriate for understanding recent developments among cooperatives,

⁶ Council Regulation (EC) No 1234/2007, establishing the Single CMO Regulation.

⁷ Regulation (EU) No 261/2012 of the European Parliament and of the Council.

⁸ Readers with an interest in the scientific literature can read articles like Hendrikse & Feng (2012) or Nilsson (2001), and/or turn to the classic reviews on the topic by Staatz (1989) and Cook et al. (2004).

we include description and assessment of important changes in legislation or company strategies that happened before 2000. An example of such change that has had a major impact on the development of F&V cooperatives is the Regulation (EC) No 2200/96 on the Common Market Organisation (CMO).

Table 1.1: Classification of cooperative research themes in the scientific literature

Themes originating at		
Member firms	Transaction relationship	Cooperative enterprise
Portfolio problem	Double monopoly mark-up	Control problem
Horizon problem	Countervailing power	Influence problem
Single origin constraint	Asset specificity	Free riding
Coordination (horizontal)	Market access / assurance	Tax benefits
Member satisfaction	Contracts	Formal/real authority
Social capital	Trust	Member involvement
Competition policy	Selection	Finance
Cooperative principles	Price volatility	Pooling
	Product quality	Inertia
	Coordination (vertical)	Diversification
	Complementarities	Board model
	Member commitment	Exit and voice
	Competition policy	Incorporation law
	Cooperative principles	Cooperative principles

Source: Hendrikse & Feng, 2012

1.6 Structure of the report

The final report of the SFC project is structured as follows. Chapter 2 describes the methodology and organisation of the project, as well as the data gathering. This is followed by two chapters that describe the performance of cooperatives in the Member States (Chapter 3) and in eight sectors (Chapter 4). That description is followed by five chapters in which we analyse the material along the lines of our three building blocks (Figure 1.1.). Chapter 5 deals with internal governance. Chapter 6 discusses the material in relation to the position in the food chain, which is extended in Chapter 7 with an analysis of international and transnational cooperatives. The Chapters 8 and 9 analyse the material from the viewpoint of the institutional environment, split in a chapter on historic, social and cultural aspects and a chapter on legal issues and policy measures. Chapter 10 presents our main conclusions and a reflection on what this learns us for the role of cooperatives in unbalanced food chains. Chapter 11 translates that into operational conclusions and recommendations.

Readers who are not interested in the methodology and organisation of the project can skip Chapter 2. Those that are roughly aware of the situation of cooperatives in Europe can skip Chapters 3 and 4 and jump directly to our analysis of different themes in the building blocks in Chapter 5 and further. Sections in these chapters that deal with a specific topic can be read rather independent from the rest of the text. Readers who have to economise on time and are only interested in the main conclusions of this project that are relevant for (European) policies should read the executive summary and Chapters 10 and 11.

2 Methodology and organisation of the project

2.1 Introduction

The project “Support for Farmers’ Cooperatives” has been carried out in 2011 and 2012 in a number of stages and with a variety of methods. As to the methodology of data collection, data analysis and presentation of results, the SFC study used a multidisciplinary approach. Data has been collected from multiple sources, both qualitative and quantitative methods of analysis have been adopted, and both narrative, argumentative and descriptive methods of presentation have been used. As much as possible, data triangulation has been used for the individual country, sector, synthesis, and case study reports.

This chapter explains how the project was organised and the methodologies used. Section 2.2 provides information on the data gathering process. These data were put into context by country reports (section 2.3), that were reworked into sector reports (section 2.4). All this information was used to carry out a number of studies at the EU level, in which the building blocks of our conceptual framework (Figure 1.1) were used as the main focus points (section 2.5). Data on individual cooperatives were used in conducting a cluster analysis. The clusters identified, interesting issues raised in the country, sector and EU-wide reports and discussion in a stakeholder workshop led to the choice of a number of policy issues and research questions that were addressed in 34 case studies (section 2.6).

2.2 Data

On individual cooperatives

Multiple sources of information have been used, such as databases, interviews, corporate documents, academic and trade journal articles. The databases used are Amadeus, FADN (Farm Accountancy Data Network), Eurostat and a database from DG AGRI on Producer Organisations in the F&V sector. Additionally, data provided by Copa-Cogeca has been used.

These centrally available data are rather incomplete concerning agricultural cooperatives. Official Eurostat statistics seem to neglect the phenomenon. We therefore have used these data as a starting point for data collection in the Member States. National (cooperative) experts have collected information on individual cooperatives by studying national publications (e.g. from cooperative councils or lobby organisations), annual reports, other corporate publications and websites. National and grey literature has been studied. In addition interviews have been conducted with representatives of national associations of cooperatives, managers and board members of individual cooperatives, and academic or professional experts on cooperatives. In nearly all cases data collection has been done by national experts in their own language.

As part of the country reports, national experts compiled a list of the top-50 agricultural cooperatives in their country, in terms of turnover (see Section 2.3). Information on market shares was also gathered. However, given the limited availability of relevant data, market shares were calculated as the percentage of the value of farm produce handled by cooperatives in a certain product. In addition, detailed data has been collected on individual cooperatives, their position in the food chain and internal governance, and some of their basic financial data.

A questionnaire was developed for this purpose [see Annex 2]. Data was collected on the top-5 cooperatives (in terms of annual turnover) for each of the eight sectors under study (cereals, sugar, pig meat, sheep meat, fruit and vegetables, olive oil and table olives, dairy and wine sectors). When fewer than five cooperatives per sector existed in a particular country, all of them were investigated. When the top-3 already covered 95% of the market share, only these three were covered in the questionnaire. The questionnaire consisted of detailed questions about the cooperative in general (such as turnover and number of members), the internal governance (such as on board structure and member influence), and on position in the food chain (such as the stage(s) of the chain the cooperative is active in, degree of vertical integration,

and the strategy adopted).

Some comments should be made on the issue whether these top-5 cooperatives (listed in Annex 3) are representative for all cooperatives in the country and sector. We acknowledge that they may not be fully representative, but we chose this strategy of data collection for a number of reasons:

- By choosing the top-5 per sector, we assumed that we covered the largest part of the sector turnover accounted for by cooperatives and the majority of farmers per sector per country.
- As the position in the food chain is an important perspective for this research project, we assumed that by taking the top 5 per sector, we most likely include cooperatives that have vertically integrated into marketing branded products.
- As the size of Member States differs significantly, the choice of the top-5 per country leads nevertheless to a sample with both large and small cooperatives⁹.
- Given the size and strategy of these cooperatives, we assumed that these were the ones that regulation and support measures have most effect upon.
- Finally, data collection on individual cooperatives is easier for large cooperatives than for small cooperatives as the former are more likely to have annual reports published.

The data on the top-5 cooperatives were inserted in a user-friendly Excel database that enables easy access to the desired type and form of information. This database has been handed over to the European Commission.

On policy support measures

Data on existing policy support measures in EU and non-EU OECD countries was collected in a three-step approach. First, information on the importance and development of agricultural cooperatives was collected (see above; for non-EU OECD countries this was done by reviewing the literature and conducting telephone interviews of key local experts). Second, policies were identified that affect agricultural cooperatives in the studied countries. Third, an expert assessment was done of the impact each policy measure has on the competitive position of cooperatives vis-à-vis their competitors. There are many types of policy measures, ranging from tax law and competition policy to direct subsidies to train cooperative directors. This makes it useful to classify policy measures into groups. McDonnell and Elmore (1987) propose the following typology of policy measures:

POLICY MEASURE TYPE	DEFINITION
Mandates	Rules governing the actions of individuals and agencies
Inducements	Transfer money to individuals in return for certain actions
Capacity Building	Spending of time and money for the purpose of investment in material, intellectual, or human resources (this includes research, speeches, extension, etc.)
System Changing	Transfer official authority (rather than money) among individuals and agencies in order to alter the system by which public goods and services are delivered

These four policy types can be further specified into individual policy measures. To direct the enquiry towards policy measures that influence cooperatives, we also used a more specific categorisation of cooperative related policies and regulations, partially based on Sexton and Iskow (1992):

⁹ This is one of the reasons that we do not compile a top-500 list of European cooperatives, also as it is highly possible that in a country the 6th dairy cooperative is larger than the 3rd wine cooperative.

- (i) cooperative legislation/incorporation law,
- (ii) market regulation and competition policies,
- (iii) financial and other incentives (e.g., tax exemption, access to favourable credit, etc.),
- (iv) technical assistance, and
- (v) other.

This categorisation facilitated a better understanding of the policies by local cooperative experts who were asked to assess the impact of each policy measure on cooperatives' competitive position on a scale ranging from -4 (extremely negative) to +4 (extremely positive) for the development of cooperatives.

The assessed public policy measures were inserted in an Excel database that enables easy access to the desired type and form of information. It includes all the information gathered in step 2 and the expert assessments of step 3. More specifically, the database provides easy access to information on the following: Country; Year; Policy type; Policy measure; Objective of the policy measure; Targeted population; Expert assessment of each policy's impact on the competitive position of cooperatives; and additional expert comments (e.g., a brief evaluation of the factors that led to the success or failure of the policy measure). This database has been handed over to the European Commission.

2.3 Country reports

Data are very useful when interpreted in the right context. The performance of cooperatives differs between Member States, as does the context in which they operate. Therefore the national experts in the project not only gathered data, but also wrote a country report to provide additional information and to comment on and analyse the data reported, in line with the building blocks of our methodology (Figure 1.1).

National experts conducted interviews with representatives of national associations of cooperatives, managers and board members of individual cooperatives, and academic or professional experts on cooperatives.

The national experts were given a very fixed format for the report with predefined sections and tables and instructions for the work to be carried out. This was done to guarantee common methodology, maximum comparability and efficiency. In line with this format, the country reports provide at least the following information:

- Description of agriculture and the farm structure in the Member State.
- Description of types of cooperatives and producer organisations, including a list with names of the 50 largest farm cooperatives.
- Data on the market share (in terms of agricultural production) of cooperatives as a group, all sectors, and per sector (calculated or based on expert judgement).
- List of the top-5 largest farmer cooperatives per sector that matter for this study (up to 95% of market share).
- List of transnational cooperatives.
- Interesting experiences, like ambiguous cases or hybrids.
- An analysis of the development of cooperatives in terms of the building blocks (internal governance, position in the food chain, and institutional environment).
- An analysis of the development of cooperatives in the eight sectors relevant in this study
- Additional information concerning possible changes in law and regulations that affect cooperatives and other producer organisations.
- List of relevant policy measures.
- An assessment of the impact of policy measures and regulations on the development and competitive position of cooperatives in the food chain.

Non-EU OECD countries

In addition to the 27 country reports, a report was written on the importance and development of agricultural cooperatives in a number of non-EU OECD countries, as well as the initiatives,

support measures, regulations and policies intended to help farmers organise themselves in agricultural cooperatives. The report also includes a thorough evaluation of the assumptions and findings presented in the literature. The focus of this particular report was on the following countries that share similar cultural or other characteristics with Europe: Australia, Canada, New Zealand, Norway, Switzerland, and USA. The main findings from these 27 country reports and the non-EU OECD countries that are linked to national aspects are reported in the next chapter.

2.4 Sector reports

The SFC study focuses in more detail on cooperatives in eight sectors: cereals, sugar, pig meat, sheep meat, fruit and vegetables, olive oil and table olives, dairy and wine. On each of these sectors a report has been written, mainly based on the 27 country reports. Additionally, an inventory of policy measures at the EU level (with the same data as for the Member States) was used. The sector reports have been written by members of the research consortium with a certain expertise in the sectors they analysed.

To guarantee comparability and improve efficiency, the writing of sector reports was also according to a fixed format. They provide at least the following information:

- Description of agriculture and the farm structure in the Member State.
- Description of types of cooperatives and producer organisations, including a list with names of the 50 largest farm cooperatives.
- Data on the market share (in terms of agricultural production) of cooperatives as a group, all sectors, and per sector (calculated or based on expert judgement).
- List of the top-5 largest farmer cooperatives per sector that matter for this study (up to 95% of market share).
- List of transnational cooperatives.
- An analysis of the development of cooperatives in terms of the building blocks (internal governance, position in the food chain, and institutional environment).
- An analysis of the development of cooperatives in the eight sectors relevant in this study
- Additional information concerning possible changes in law and regulations that affect cooperatives and other producer organisations.
- List of relevant policy measures.
- An assessment of the impact of policy measures and regulations on the development and competitive position of cooperatives in the food chain.

The main findings of these eight sector reports are reported in Chapter 4.

2.5 EU synthesis reports

The 27 country and 8 sector reports were synthesised at the EU level, with the main purpose to gain more insights related to the building blocks of our methodology (Figure 1.1.). One report dealt with Internal Governance, another with Position in the food chain. Concerning the Institutional environment, three analytical reports were produced: one on social, cultural and historical aspects, one on legal issues and one on policy support measures. A sixth report dealt with transnational cooperatives.

EU-level synthesis reports are based on the country and sector reports, and thus on data collected in the spring of 2011 in the 27 EU Member States. For some of the EU synthesis reports, additional data has been used. For instance, for the EU-wide analysis of social, cultural and historical influences on agricultural cooperatives, additional data from the Eurofound survey on “Living Conditions and Quality of Life in Europe” and the Hofstede indicators¹⁰ have been used.

¹⁰ Available at www.geerthofstede.nl

While most EU syntheses reports are mainly descriptive, in some of the reports a more quantitative approach was used. For instance, in the “EU-wide analysis of internal governance” descriptive statistics have been presented describing country and sector differences in terms of the internal governance characteristics of cooperatives¹¹.

For the EU-wide analysis of Legal Aspects, data from the 27 country reports were used, as well as data on the legal business form of the cooperative available through the “Study on the implementation of the European Cooperative Statute”.¹² On the basis of the data collected, a comparative overview has been made of the legal measures and tools that are considered to affect the economic performance and development of agricultural cooperatives, assessing the main question of how law in general and business organisational law, tax law and competition law in particular contribute (or not) to the ingredients for the success of agricultural cooperatives. The analysis in particular provided legal input on the drivers and constraints for the development of cooperatives with respect to the following study areas:

- the fiscal incentives or disincentives at regional, national and/or EU-level,
- the legal aspects including those related to competition law, and
- the internal governance of agricultural producer organisations and cooperatives.

The EU synthesis reports have been written by members of the research consortium with a certain expertise in the topic analysed. The main findings of these six reports are reported in the Chapters 3 and 5.

2.6 Case studies

The fact finding in the project was concluded with 34 case studies. The EU-wide analysis of country and sector reports as well as a cluster analysis and the results of a stakeholder workshop in November 2011 provided the basis for selecting the 34 case studies, 15 of them on transnational cooperatives.

The cluster analysis was carried out on the individual data on the 500 cooperatives gathered (see section 2.1). It revealed eight clusters with distinguishable profiles:

- A. Federated (second-tier) cooperatives
- B. Supply cooperatives
- C. Bargaining cooperatives
- D. Specialised processing cooperatives
- E. Large agribusiness cooperatives
- F. Niche market cooperatives
- G. Emerging cooperatives
- H. Regional specialties cooperatives

In Figure 2.1 these clusters are shown in a diagram suggesting a life-cycle for at least some types of cooperatives.

¹¹ Details on the statistical methodologies used can be found in the relevant synthesis reports.

¹² This study was carried out by EURICSE, CooperativesEurope and the EKAI Centre on behalf of the European Commission, DG Enterprise and Industry, and was published in November 2010. It contains data on the implementation of the European Cooperative Statute in all 27 Member States. Also, it provides information on the legal business form of the cooperative, providing very detailed information for the 27 Member States on the legal (including tax) aspects of cooperatives, based on national experts' legal analysis and on interviews with legal scholars, board members of cooperatives and practitioners.

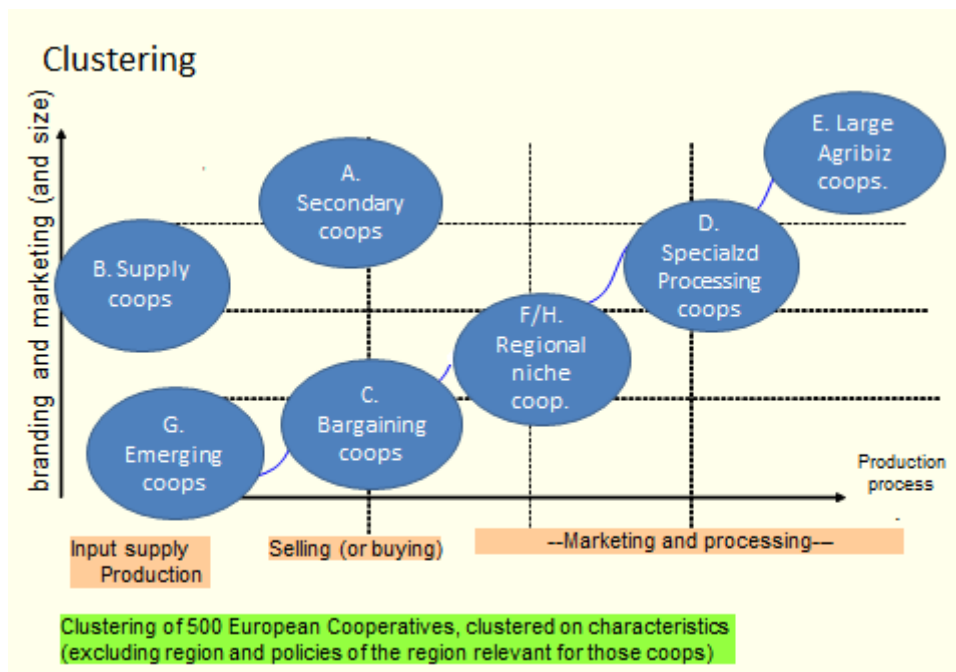


Figure 2.1 Results of a cluster analysis

Based on the results of the country, sector and EU synthesis reports, a number of relevant policy issues and research questions were identified in a stakeholder workshop. It was argued that especially the issue of the unbalanced food chain was important (and therefore less attention was paid on input supplying cooperatives) and that it would be fruitful to differentiate between types of cooperatives and their typical problems. Table 2.1 lists some of these problems per type of cooperative and summarises that discussion.

Next, using the know-how of the consortium partners, 34 cases were selected. The case research was guided by two internal methodology notes, one for the national cases and one for the transnational ones. In these methodology notes a number of hypotheses were developed, on the basis of literature and of the findings of the country and sector studies. These hypotheses have been used to guide the data collection and data analysis of the case studies. As the case studies mainly used a qualitative approach, no statistical testing of the hypotheses was possible. By using the same hypotheses in more than one case study, and one case study often containing descriptions of two or three cooperatives, comparisons can be made over countries, sectors, regions and, sometimes, even individual cooperatives. By clustering case studies and/or hypotheses, a comparative meta-analysis over the cases has been performed by the research team.

As to data collection in individual case studies, multiple data sources have been used. First, secondary data was collected from academic and professional literature, EU legislation, popular press, various archives and websites. Primary information has been collected through personal interviews with managers and members of the Board of Directors (BoD) of the cooperatives focused upon each case. Drafts of the case study reports have been circulated to the interviewees and their comments were solicited.

Table 2.1 Typical problems for certain types of cooperatives, as discussed in the stakeholder workshop

Type of Coop	Critical Success Factor	Typical problems
Emerging Coops	Farm Efficiency Create market Reduce Agency	Trust Leadership Transparency
Bargaining Coops	Market power	Member commitment
Regional Niche Cooperative	Exploit 'terroir' Know how local market	Capital and Finance Professionalization Governance
Specialised Processing Cooperative	Cost Efficiency	Capital and Finance Professionalization Governance
Large Agribusiness Cooperative	A-Brands and volume for chain power	Optimal hybrid form Membership involvement

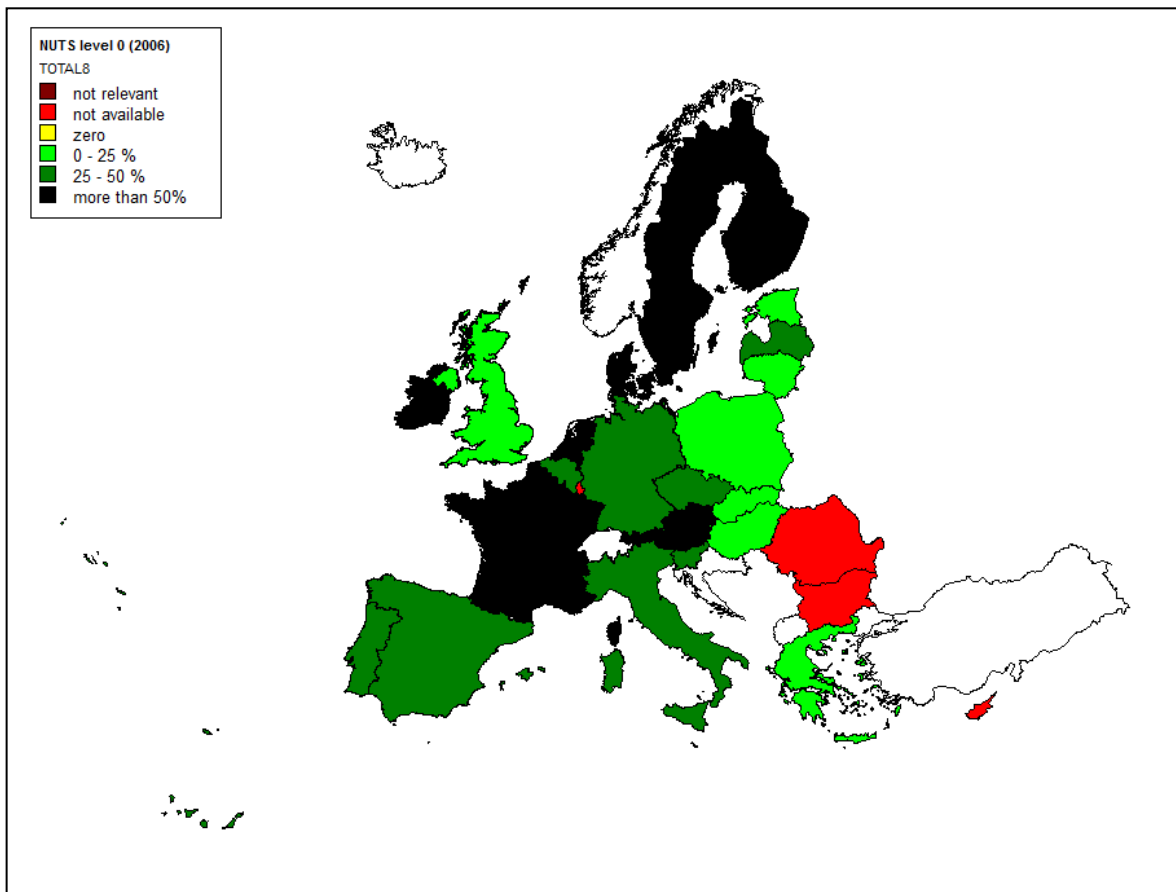
The results of the case studies and the meta-analysis have been integrated in the Chapters 3 and 5 to illustrate, deepen and widen the analysis from the EU-synthesis reports.

3 Facts and figures of cooperatives in Member States

3.1 Introduction

In this chapter we present, discuss, and summarise the results of our fact finding in the 27 Member States. Additional details can be found in the country reports (Annex 1). Figure 3.1 (consisting of a map and a bar chart) shows the relative importance of cooperatives in all Member States, based on the “SFC Cooperative Index”: the estimated market share of all cooperatives at farm gate sales level weighted for eight sectors. Hybrids (see Chapter 5) like the German sugar cooperatives and the Dutch slaughterhouse company VION have been left out of this calculation. Farm gate sales handled by an IOF owned by an international or transnational cooperative have also not been included.

The map shows that there are large differences between Member States. Cooperatives have a high market share in countries like Denmark and Finland, but much lower in countries like Estonia or Spain. The bar chart shows the data for each of the Member States. For UK, Romania, Bulgaria, Luxembourg and Cyprus data are sketchy or not available. The average market share of all agricultural cooperatives in the EU is 40%.¹³



¹³ The calculation of market share of all cooperatives is not very sensitive for the quality of data from an individual member state. A calculation for EU-22 that excludes the countries UK, RO, BG, LU and CY on which data is weak or non-available and if we would treat German hybrids (such as in sugar) as cooperatives, the market share of farm gate produce marketed cooperatively would be 45% instead of 40%. Excluding the new member states, Greece and Portugal, the market share would be exactly 50%, closer to the percentage often quoted by the North-West European cooperative organisations, in which also some hybrids and sourcing by daughter-IOFs is usually included.

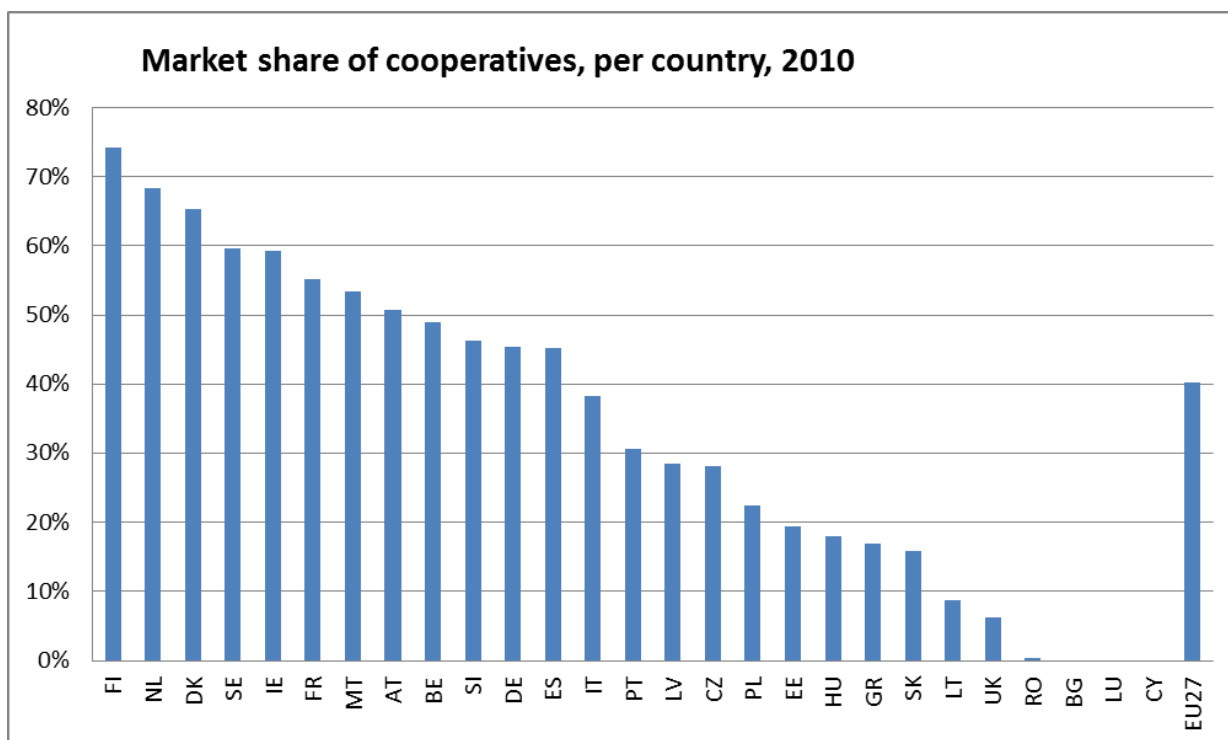


Figure 3.1 SFC Cooperative Index: Market share of all cooperatives, weighted for 8 sectors.

Another way of calculating the importance of cooperatives is by taking the number of members of cooperatives and dividing them by the number of agricultural holdings. The result of this calculation can then be transformed into a score, for each country, on a scale of one to five. Unfortunately, we did not have sufficient data for all countries to do this calculation. For those countries we did not have hard data, we used qualitative information on cooperative membership. On the basis of this information we estimated a score. These scores are called member intensity. Figure 3.2 presents a map of Europe with the score on member intensity for each of the EU Member States. Although the results should be considered with some care, the map does give a nice picture of relative importance of cooperatives across countries.

The next section discusses the findings in more detail. We concentrate on the general picture concerning the cooperative performance in the Member States (market share, size), their role in the economy and food chain and how this is linked to institutional issues and history. Less attention is paid to the individual sectors, which is the topic of next chapter.

The *tour d'Europe* starts if for no other reasons than paying a tribute to Friedrich Wilhelm Raiffeisen, from the German speaking Member States and then focuses on each of the Member States in a clockwise fashion starting with Denmark. We have deliberately chosen to handle all countries in one long section and not group them in Northwest, East and South. Although there are certainly similarities within these groups, differences are sometimes much larger. Small summaries do not do justice to all the material we gathered. For each country an individual report is available (Annex 1).

In addition section 3.3 summarises the information on the evolution and role of cooperatives in other selected OECD countries which is also presented in more detail in a separate report.

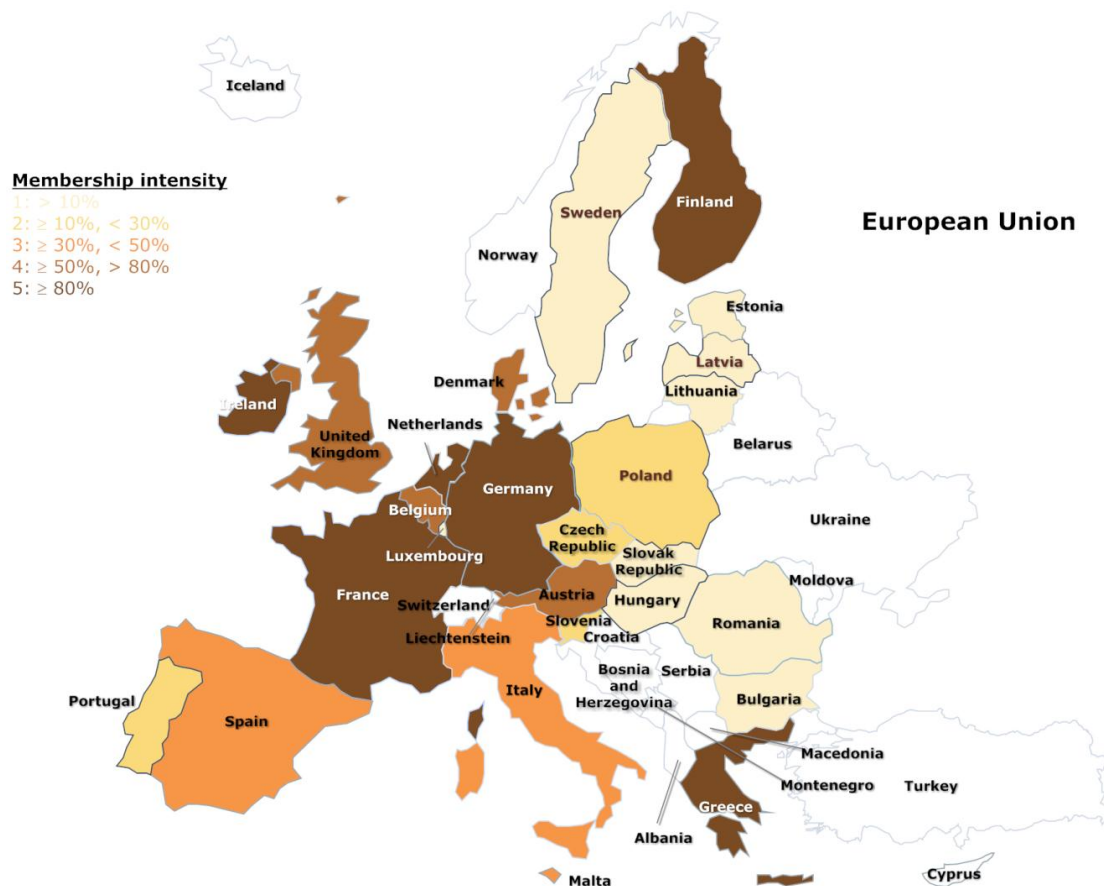


Figure 3.2 Member intensity

3.2 Main facts per Member State

Germany

Cooperatives are widespread in Germany. Almost every farmer is a member of one or more cooperatives, but also in other sectors like banking, housing and even retail the cooperative organisation form is important. Nevertheless in many agricultural sectors also investor-owned firms (IOFs) have important market shares. Germany is a country with a cooperative system that is rich in tradition and highly developed. Foreign transnational cooperatives play a significant role in some sectors. In former East-Germany many agricultural production cooperatives are active, where members bring in land and labour (see Chapter 8).

The German cooperative organisation is characterised by the fact that the competitiveness of the locally active primary cooperatives is enhanced by regional and central business organisations and by federated cooperatives, some of them active internationally. A typical element in the governance of cooperatives is that every cooperative must be member of an auditing association. Another element is the Marktstrukturgesetz that allows some collusive behaviour among producer organisations (EZGs) if that leads to a better tailoring of the supply and marketing of agricultural products to market requirements. Experience and research suggest that there may not be “one best way of organising” food supply chains: in Germany many different models for organising the cooperative are used. In almost all cooperatives, management is delegated to professionals who may or may not be members of the cooperative. The most important policy measure are the cooperative legislation and the tax law, the latter treating the agricultural cooperative as an extension of the farm.

Austria

Austria shares with Germany the importance of the cooperative sector, especially in agriculture, and some of the institutional characteristics, like the mandatory membership in an auditing organisation. Some large cooperatives like BayWa and Südzucker/Agrana are active in both countries. But there are also important differences. For instance, the Austrian dairy sector has hardly any IOF, with more than 100 cooperatives and producer organisations that often have a regional niche focus strategy. In all sectors a process of concentration can be observed. Austria's cooperative system has a long tradition and dates back to 1873. Besides the cooperative law and the tax system also the competition law is viewed as important for the development of cooperatives.

Denmark

Denmark seems to have a cooperative nature in its DNA. That goes back to the last two decades of the 19th century, when a big transition took place. The enclosure movement, the cultivation of new land (that had been idled since the black plague in the Middle Ages) and the flooding of the international market with cheap grains forced Danish farmers to innovate and move from grain to livestock production with butter and bacon for overseas markets (especially the UK). The establishment of cooperatives played a decisive role in this transition and they have earned their place in Danish agriculture since then. In dairy and pig meat cooperatives have a dominant position; Arla Foods and Danish Crown are internationally operating and well-known businesses.

Interestingly, there is no cooperative law in Denmark. Governance rules can vary a lot among cooperatives. Their own statutes (bylaws) are instrumental in determining the internal governance structure. Basically, the cooperative principles are in use (e.g. one man, one vote). The size of the cooperative and the role of the cooperative in the food chain affect the internal governance choices. In large cooperatives the governance structure consists of a Member Council (Board of Representatives) that elects the Board of Directors. The members are elected in regional meetings and there are also rules concerning representatives from different product groups. Another typical phenomenon is the complicated structure of daughter companies, especially in cereals and supply cooperatives. One of the big issues is equity raising and attracting non-member investors. Thus far, large Danish cooperatives have decided to maintain their cooperative status, although Danish Crown has some non-member capital investors and Arla Foods is also seeking to attract institutional investors.

Sweden

Sweden shares the Scandinavian cooperative attitude (also in banking, forestry, housing and consumer cooperatives), but several of its agricultural cooperatives merged into their Danish or Finnish competitors (Arla Foods in dairy, HKScan in pig meat). The exception is the cereal and inputs supply cooperative Lantmännen, a large international cooperative, active in 18 countries. The acquisition of many Swedish food processing firms by foreign competitors is, at least partially, explained by the adoption of inefficient structures in the agriculture and food sectors before the country liberalised its economy and entered the EU in the mid-1990s. As a result the production volume fell drastically in the subsequent years and there have been implemented immense restructuring measures (mergers, closed plants in the processing industry, geographical redistribution of primary agriculture, etc.). Legally, cooperatives are treated in the same way as any other legal business form. Further, the legislation enables cooperatives to choose the internal governance that fits their needs.

Finland

The founding fathers of cooperatives in Finland, in the beginning of the last century, saw their contribution in light of the struggle for independence from Russia. Pellervo, the Confederation of Finnish Cooperatives, was established in 1899. Today Finland claims to be the most cooperative economy in the world and recently cooperatives of expert networks in services have gained some popularity. The cooperatives have a very significant role in the food chain in Finland,

market shares are especially high in dairy (with Valio, federated cooperative) and meat (with transnational and partly stock market listed HKScan). Retailing in Finland is very concentrated; the two largest chains have a combined common market share of more than 80%. The internal governance varies among cooperatives, according to size. Cooperatives have a strong business orientation.

Estonia

Although Estonia had already a cooperative mortgage society in 1802, far before the Rochdale and Raiffeisen innovations, today cooperatives are a marginal phenomenon, even in agriculture. There are about five dairy cooperatives (of which one is also active in Russia), a vegetable cooperative, a cereal cooperative, a pig meat cooperative and an animal breeding cooperative. Only in animal breeding and dairy there is a substantial market share. Estonia has a very liberal, open economic system, in which private farms have to compete in global food markets. Within that environment, Estonian farmers have been able to start up cooperatives after the regained freedom in 1989. Since then hundreds of new small cooperatives have been established, but most of them have gone bankrupt or into liquidation.

Latvia

Also in Latvia the cooperative system has a long history, with a very difficult period of transition after the communist regime collapsed. Russia was the biggest export country, and that was replaced by cheap import products into Latvia at the moment that consumption declined. This led to a collapse of the (socialist) cooperatives, but since then more than 100 cooperatives have become active – currently there are about 50. In 2002, the Latvian Agricultural Cooperatives Association (LACA) was established, with the aim to promote the development of agricultural cooperation. About one third of the milk and cereals are marketed by cooperatives. Farmers more and more realise that cooperatives can be an efficient and profitable way of marketing their products. There are examples where cooperatives hire a professional manager, but most of the decisions are made by the board of directors and the general assembly of members.

Lithuania

Lithuania shares a similar historic path with its neighbours. About 400 cooperatives play a significant role in dairy and cereals as well as in fruit & vegetables. People in the countryside tend to cooperate in informal ways by offering their help to the neighbours when needed; including help in field work, providing machinery services and cooperation during the harvest. However, that does not necessarily leads to membership in a cooperative. A detailed study in dairy reveals that farmers are proud of the dairy cooperatives that they set up in recent years (see Chapter 8). Small-size farmer cooperatives are dominant in Lithuania. In 2007, 44% of the farmer cooperatives had only five members, while only seven cooperatives had more than 500 members. About three quarters of the cooperatives have open membership policy, some apply entry criteria and 8% is closed to new applicants. In one out of twelve cooperatives the board of directors (that has on average 5 members) includes non-member professionals. According to the Lithuanian law, cooperatives have a one-tier board structure. In some cooperatives, members with higher than average levels of patronage receive a quantity premium.

Poland

Polish agriculture was less influenced by the socialist plan economy than some of the other Central and East European countries. Family farming survived (with the exception of the former German areas), and the cooperative sector was able to operate more or less according to the cooperative principles, although strongly influenced by the state. With the transition most of the largest cooperatives in primary agriculture were liquidated or converted into IOFs; others lost their members and collapsed. Currently, cooperatives have a bad image as being an obsolete structure.

Nowadays cooperatives command a large market share (> 70%) only in the dairy industry. In the last decade producer organisations and producer groups in the fruit and vegetables sector

have been formed that now have about 10-12% of the market. To a smaller extent new producer organisations are also set up in the pig sector. Some Scandinavian cooperatives are active in Poland. Internal governance in cooperatives is seen as problematic by experts. Old habits from the socialist past remain. In many cooperatives, there are no young people among the board members or management staff. The prevailing corporate culture in some of these organisations centres on survival, not offensive entrepreneurial ventures. As a result, crucial, long-term strategic decisions are constantly postponed. New cooperatives and those in dairy work more often with professionals and are more “business-like” in their operation. After the EU accession in 2004, more subsidies and financial schemes were introduced, supplementing the general provisions of the Law on Producer Groups. As a result, more new groups appeared, but some of them might be too much subsidy driven.

Czech Republic

In the Czech Republic the land reform in the Interbellum led to a large number of cooperatives. Producer (marketing) organisations started re-emerging in 1994. Since 1999, they have been supported by various policy measures. Marketing cooperatives are, by far, the most common form but not the only one. Limited liability companies are also active. Currently, producer organisations in Czech Republic adopt a two-tier structure. At the bottom level, there are producer organisations and producer groups unifying primary agricultural producers. These producer organisations can be either agricultural cooperatives or adopt any other legal form (usually limited liability companies or joint stock companies). At the top level, there are national cooperatives. Cooperatives are important in hops, dairy, fruit & vegetables, and – to a lesser extent – in sheep and pig meat. Also agricultural production cooperatives continue to be important.

Slovakia

In Slovakia, as a result of the transition process, agricultural production cooperatives play an important role. Less than 600 of such cooperatives farm 52% of the land (Chapter 8 provides more details on this development). There are also cooperatives and producer organisations for collective bargaining on product sales in the market. Their market share is highest in the dairy industry (25%), followed by potatoes (18%) and cereals (16%). They often represent only a few (5 to 7) agricultural cooperatives. Mainly large cooperatives are members of bargaining producer organisations.

Hungary

Large scale farming has also been preserved in Hungary, but here based on the privatisation of land via a voucher system. Concerning the food supply chain the privatisation resulted in the property rights ending up with IOFs that now have a dominant market position, while cooperatives account for a very low share. Although the number of cooperatives is decreasing, there are still 890 traditional agricultural production cooperatives, and about 330 new emerging marketing cooperatives and producer organisations (including producer groups), mainly in fruit and vegetables, cereals and oilseeds, pigs and poultry. Their concentration is limited with low levels of second-tier organisation. The capitalization is very low as well and access to credit is very hard for agricultural cooperatives. Moreover, there is a low level of trust and willingness to cooperate in the agricultural sector in general. The experiences with these cooperatives are mixed. Some play an efficiency-maximising role when qualified, skilful managers are able to guarantee good prices and liquidity by paying in-time. In other cases, free-riding members deliver directly to customers thus bypassing the cooperative. Avoiding paying taxes sometimes explains this behaviour. There are also cases where successful cooperatives grew too fast and went bankrupt due to inefficient financial management. A new cooperative law will come into force in 2013.

Romania

Romania, once considered the breadbasket of Europe, it is at present a net importer of products. After privatisation agricultural associations and – since the law of 2004 – cooperatives have been established. The associations are more or less a follow-up of the socialist cooperatives, and are now disappearing. The number of cooperatives is low and also declining, from 108 in 2005 to 68 in 2010. All of them were active in farming, not in processing or marketing (besides their own products). In addition there are 150 producer organisations and producer groups, mainly in the fruit and vegetables sector. Although a marginal form, agricultural cooperatives have attracted the public attention in recent years because of tax exemptions available to them, supported by tax reductions and access to European funds, and also via a large media campaign.

Bulgaria

Bulgaria has a tradition in cooperatives, however not strong enough to change the production structure after the radical liquidation of state and collective farms. As Bulgaria had implemented land reforms before collectivisation, the land ownership after restitution is fragmented. This has led to a dual agricultural structure: numerous semi-subsistence farms (pensioners) and agricultural production cooperatives that include many absentee land and asset owners. These cooperatives rent land from many owners, organise land consolidation and provide services for small-holders (including market access). In many regions they also perform important public tasks, like road maintenance, kindergarten, inexpensive canteens – functions that in other ex-socialist countries have been handed over to the government (see Chapter 8).

Slovenia

Cooperatives in Slovenia were developed in the 19th century and remained important in the Yugoslavian socialist economy. The cooperative movement shows a positive development in recent decades. Market shares are high in dairy, cattle and fruit & vegetables. The most commonly adopted governance model includes the so-called president of the cooperative at the top (elected by the general assembly of members) and a supervisor committee. Alternatively, the president is replaced by a management board, also elected by the general assembly. The latter can also choose to have non-members elected into the management board (most common in larger cooperatives). However, the president is mandatorily a member-owner of the cooperative. If a director is appointed, it is very often an outside expert.

Greece

Greece can report examples of diverse cooperative arrangements since the ancient times. During the 18th and 19th centuries however, cooperation adopted more formal organisational structures. It is striking that cooperatives in other sectors (like supply cooperatives for pharmacies or taxi drivers) are very successful, where agricultural cooperatives have much more a political character (Greece is probably the only Member State where the political affiliation of board members is sometimes published, once a legal obligation) and are struggling. Greece also has a unique facility in five “mandatory cooperatives” of which one holds an almost monopolistic position in the mastic gum products market.

F&V, wine and olive oil are the most important sectors, although the largest cooperative is a poultry cooperative that has a 30% market share. Many cooperatives are rather small. In some secondary cooperatives, even some with a relatively high business volume, the professional manager is merely an assistant to the chairperson who acts as the chief executive. In terms of strategies adopted, agricultural cooperatives are fairly defensive organisations (see Chapter 6 for a detailed analysis on strategies and structures in cooperatives in several of the Mediterranean countries). An important development since the country report was written is the enactment of a new law, which makes mandatory the conversion of all second-tier cooperatives into either first tier cooperatives or farmer-controlled IOFs.

Cyprus

In Cyprus many cooperatives have been set up under British rule and the sector developed strongly after independence. Cooperatives in Cyprus are registered as limited or unlimited enterprises under the Cooperative Law. In the accession process of Cyprus into the European Union, the concepts of Producer Organisations (PO) and Producer Groups were introduced. Cooperatives dominate in cereals and POs handle about a quarter of fruit and vegetables (2007 data). The cooperatives are governed by a non-executive Board of Directors and an employed secretary / manager, almost always a man and sometimes a member of the cooperative, with executive powers and no voting rights on the board. He is responsible to implement board decisions. The manager / secretary may have other people working under him and helping him carry out the work. The members of the Board of Directors are elected during the Annual General Meeting and serve for a three year's renewable term without any benefits.

Malta

The cooperative sector in Malta is relatively young: the poverty after the Second World War induced the Colonial Government to stimulate farming and promote cooperatives. Malta now counts 16 active cooperatives and nine producer organisations. Milk producers and pig breeders are all organised for many years in a strong cooperative. Farmers in the fruit and vegetable sectors have many different but smaller cooperatives and producer organisations that have a market share of about 20%.

Italy

The Constitution of the Italian Republic, dating back 1948, explicitly promotes cooperatives in article 45. Agriculture and the food industry count 11,000 cooperatives, 14% of the Italian total. Most agrifood cooperatives are associated with one of the five recognised national associations. Cooperatives are important in wine, fruit & vegetables (both around 50% market share) and dairy (42%). In olives and olive oil the market share is low and declining (5% in 2010). Most agrifood cooperatives have adopted the "one-tier board structure" with supervisors and executives in one board of directors. However, since the 2003 company-law reforms, it is now possible to adopt the "two-tier board structure". In the last decade laws have been designed so as to promote the integration of the processing and marketing activities of cooperatives and the production activities of members. The EU legislation on producer organisations has been beneficial, too.

Spain

In Spain, where once cooperatives were heavily promoted by the Catholic Church to counterbalance the socialist worker movements, cooperatives are generally viewed by the administration as part of the "social economy", in which social and economic aspects are both important. Spain is characterised by important regional political, economic and social differences and there are certain agricultural subsectors which are dominant in one region and non-existent in others. Spain has both a national cooperative law and regional or autonomous community cooperative laws. By virtue of the sheer volume of cooperative laws and policies at the autonomous community level, there is little united policy orchestration which would be ideal in confronting an increasingly competitive and globalised marketplace. Most cooperatives are incorporated at the autonomous community regional level to take advantage of regional policies and incentives and subsidies which are for the most part administered by the autonomous communities. Resulting inconsistencies between regions complicate interregional cooperation, thus ultimately inhibiting growth strategies and at times internationalisation. Financial constraints are common in cooperatives, and even more so when these cooperatives are "confined" within regions. Policy direction is at times contradictory. There are about 3,500 agrifood cooperatives with more than 67,000 workers, Andalusia being the autonomous community with the highest number. Market shares are high in wine and olives & olive oil (about 70%), substantial in dairy and fruit & vegetables (more than 40%) and still about a quarter in the other sectors. In Spanish cooperatives the three obligatory governance bodies are:

the General Assembly, the Management Board and “Intervenors”. The latter body has a limited supervisory and accounting role. Cooperatives are mainly active in collecting and forwarding member products to the next stage of the food supply chain, as well as the procurement of supplies. The largest cooperatives are much more involved in processing and marketing branded products. This situation is beginning to change as there are more integration and concentration initiatives, but there is still much work to be done to address the atomization of Spanish agricultural cooperatives.

Portugal

The Portuguese cooperative movement has its roots in the 19th century, linked to the labour movement, but the dictatorship period was characterized by formal hostility to cooperatives (although informally the government was more tolerant). The 1974 revolution gave rise to a strong cooperative expansion but since the mid-1980s a period of significant cooperative failures occurred, as a result of intense market competition. Today cooperatives play a relevant role in the supply chains of milk, wine, and fruit and vegetables. Portuguese agricultural cooperatives are by law structured in a two tier internal governance-system (thus, with Board of Directors and Supervisory Board (unless there are not enough members to fill both governance bodies, as may be the case in federated cooperatives; then one governance body is sufficient). About 95% of the products processed by dairy cooperatives are sold in the domestic market or exported to former colonies. Although there are some well-known brands of cooperative wines, in general, cooperatives operate in the low-price segment of the consumer market. Also for olive oils, cooperatives have few consumer brands.

France

Cooperatives are an important aspect of French agriculture. Fifty per cent of the farmers are members of a Coopérative d’Utilisation du Matériel Agricole (CUMA), that buy and share farm equipment. In many sectors (much) more than 50% of the products are handled by cooperatives, with exceptions in wine, eggs and beef (where cooperatives are still relevant with more than a third of the market) and vegetables (25%). Compared to some other countries the French dairy sector is characterised by a large market share (over 40%) of IOFs. The list of cooperatives includes well-known names like Champagne Cereales, Tereos (Sugar), Sodiaal (dairy), Agrial (multipurpose, inputs) and Limagrain (an international seeds producer).

Initially, cooperatives simply collected products from their farmer members but, over the years, they have increasingly invested in first- and second-level processing. In a number of cases this investment was defensive, to “rescue” a sector and step in where an IOF decided to sell out. Most of the processing is organised via subsidiaries, and the French cooperative legislation has been updated rather frequently over the last decades to make such new methods of internal governance possible. There are only two possible modes of managing the cooperative: either a board of directors composed of elected farmer members, with a chairman and a managing director, or –seldom used - a structure with two separate boards (management and supervisory board). France is unique in giving its cooperatives a territorial constraint: cooperatives need to obtain official territorial authorisation for the right to operate, within the economic sector applied for, and within the limits of a specific and restricted territory.

Luxemburg

In Luxemburg cooperatives are, at least statistically, not very important. Dairy (Luxlait) and the wine cooperatives on the Mosel river are the main exceptions, as well as some smaller ones in vegetables, cereals and meat. However there can be some underreporting as several farmers do business with (but are not necessarily a member of) cooperatives of the neighbour countries. For instance, several hundreds of dairy farmers are member of the German cooperative Milch-Union Hocheifel (MUH), that was in mid 2012 in a merger process with Arla Foods of Denmark. There is no specific regulation for agricultural cooperatives. Cooperatives are regulated by the commercial companies act (1915).

Belgium

Belgium is a country with a long history of cooperative entrepreneurship (that was embedded in the socialist labour movement and the Christian farm movement) and quite a few large cooperatives. Cooperatives like the Mechelse Veilingen (a vegetable auction) and Milcobel (a dairy cooperative) are large, internationally known organisations. The National Council for Cooperation, recognised by Royal Decree, accredits cooperatives that operate according to principles of cooperative governance. Accreditation gives some social and fiscal advantages. The market share of cooperatives in Belgium is rather diverse, with high percentages in F&V (83%), followed by dairy (66%) and pig meat (more than 25%), but very low or non-existing in sugar and sheep meat (while for cereals we do not have data). Bargaining associations are active, among others in the vegetable processing industry. The sugar factories are run on an IOF-basis by French and German cooperatives. In contrast to (or in line with) these market shares, Belgium has an active policy to promote cooperatives, and there is a large number of relevant support measures. This is partly due to the federal character of the country (where Wallonia has more cooperatives, but the Flemish ones are larger).

The Netherlands

Many cooperatives in the Netherlands can trace their origins to the end of the 19th century, with an agricultural crisis and reaction comparable to the Danish one reported above. There has been a strong merger process between cooperatives leading to only a few or even one cooperative per sector, and federated cooperatives disappeared (except in banking where Rabobank is an important player). In several sectors (like sugar and starch) IOFs have left the sector, where in others (like slaughterhouses) cooperatives have been less successful. Several cooperatives are international or even transnational (like FrieslandCampina). The Dutch cooperative law is very flexible concerning internal governance and attracting equity from members or others. This has led to a large array of solutions in the bylaws that fit the cooperatives' strategic needs. It often includes a legal separation between the cooperative association and the cooperative firm. Producer organisations play an important role in the fruit and vegetable sector, and show innovative dynamics in product development and marketing. They are closely followed by the Competition Authority. The tax law treats cooperatives as an extension of the farm, and thus surpluses are taxed at either the member or the cooperative level but never at both. This policy has benefitted the capitalisation of cooperatives in the early stage of their development.

United Kingdom

From Rochdale on, the cooperative movement in the UK was dominated by the labour movement in retail. Data on cooperatives in the agrifood industry are scarce and outdated, but suggest considerable market share (in terms of farms' produce handled) in fruit & vegetables, milk, and to a lesser extent in pig meat and cereals. In cases like milk, this situation is the result of the fact that the abolished marketing boards turned into cooperatives. The sugar sector is run by an IOF, but the National Farm Union acts as a bargaining association. The devolution of powers and authority in different degrees to Wales, Northern Ireland and Scotland, as well as delivery of much economic policy via the Regional Development Agencies within England created differences in the support for agricultural cooperatives.

Ireland

The second half of the 19th century, the post-famine period, was a period of rapid changes in Irish agriculture, marked by the growth in livestock production and the introduction of science into agriculture. Today there is great variety in the Irish agricultural cooperatives especially in terms of size, structure and activity. Some have evolved to resemble bargaining associations, limiting themselves to negotiating with buyers; at the other extreme there are Irish agricultural cooperatives operating on the global market with subsidiaries in both Europe and the U.S. Some of these have converted into a Public Limited Companies (PLC) in order to finance this growth. Kerry Cooperative Creameries set this example and now it holds a fifth of Kerry Group PLC, with

a free float of the rest in the Stock Exchange. Including such hybrids, the dairy sector is nearly 100% dominated by cooperatives while cooperatives control two-thirds of the livestock sector.

3.3 Other OECD countries

In non-EU OECD countries that share similar cultural or other characteristics with Europe (Switzerland, Norway, Canada, USA, New Zealand, Australia) cooperatives also play an important role in the food chain. All of them have some large cooperatives, and especially the USA hosts many very large cooperatives. There are large differences in economic and agricultural policies between these countries. For instance New Zealand has a very liberal economic policy, an export-driven agriculture and hosts at the same time large, internationally operating cooperatives (e.g., Fonterra in dairy, and Zespri in kiwifruit). Switzerland, a food importer with a changing agricultural policy that stresses the positive externalities of agriculture, has important consumer cooperatives, but agricultural cooperatives are less developed. Among these six countries, the intensity of governmental support for cooperatives differs, in descending order: Canada, the USA, Norway, Australia, New Zealand and Switzerland.

The performance of agricultural cooperatives is affected by several parameters that interact but are not equally important in all countries. The most influential parameters seem to be the formal institutional environment, either directly or indirectly (laws, regulations, measures, initiatives, etc.) and the informal institutions that play an important role in shaping the environment in which cooperatives operate. Both formal and informal institutions are shaped by the prevailing culture and socio-economic conditions, as well as historical path dependencies. The dominant paradigm regarding the role and expectations from agriculture and farmers has a crucial impact on the overall agricultural policy and regulatory frameworks adopted by each country. Farmer cooperatives and support towards them is crucially affected by this paradigm. Another significant parameter refers to the structural characteristics of agriculture and farms. For example, in countries with larger, capital-intensive farms, support policies may be less necessary to spark efficient collective entrepreneurship.

3.4 Concluding remarks

The overview of cooperatives in European countries shows that for a long time all Member States have a cooperative tradition. But with differences of origin: sometimes it was the labour movement, in other regions the Catholic Church that played a key role. In some countries (Denmark, the Netherlands, Ireland) the cooperative history is very much linked to important transitions, crisis and hardship. In others (like Finland) it is linked to the struggle for independence – these memories seem to help to sustain a positive collective attitude.

General economic attitudes and political views matter, too. The liberal attitude and abrupt changes have not benefitted cooperatives in, e.g., Sweden and Estonia. At certain times some political regimes have been hostile to cooperatives (e.g. the dictatorship period in Portugal and Spain). Inefficient policies and opportunistic cooperative leaders may cause severe failures, as suggested by the Greek experience. And of course there is the socialist-experience that until today has a major influence in Central and Eastern Europe. It is amazing how differently the transition processes after 1989 have worked out (see Chapter 8 for a detailed analysis).

The overview also shows how different national cooperative legislation is, and how this has affected internal governance models. It raises the important question to what extent internal governance matters for the performance of the cooperative, and if this is relevant, what that implies for cooperative legislation (see Chapter 5).

Concerning the market shares of cooperatives the overview shows important differences between countries (which begs for explanations noted in the institutional environment, including legal, historic and social aspects) and between sectors. Dairy and fruit & vegetables are often sectors with important market shares for cooperatives. But even in dairy there are large differences between, e.g., Austria and Denmark versus France and Germany. Differences are even bigger if one looks to sectors like sugar (e.g. Belgium versus France and the Netherlands) or

olive oil (Italy versus Spain). In the next chapter we focus in more detail on eight sectors.

In a nutshell, cooperative development in Europe is sometimes characterised by successful internationally oriented IOF types of businesses in North-western Europe, and more traditionally and social oriented, struggling with internal governance issues, in the Mediterranean countries. Cooperative development is rather problematic in New Member States due to the socialist heritage and a lack of trust and leadership skills; and although it is tempting to use stereotypes, the description in this chapter shows that the reality for policy makers is more complex. The stereotypes are outright wrong for many cooperatives - especially for many successful cooperatives in the South and East of Europe. It seems that there are quite diverse national issues and challenges.

4 Performance of cooperatives in eight sectors

4.1 Introduction

Mainly based on the inquiries in the Member States (Chapter 3), this chapter discusses the performance of cooperatives in eight sectors for all of the 27 EU Member States: dairy, pig meat, sheep meat, wine, fruit and vegetables (F&V), olive oil and table olives, sugar, and cereals. Of course, not all products are relevant in all Member States; olives are not cultivated in Finland. For each sector a detailed report is available (see Annex 1).

For each sector market shares of cooperatives are discussed in detail. In addition, we elaborate on the position of cooperatives in the food chain and link this with the characteristics of the product, the structure of farming and agricultural policies where relevant. Pertinent information on the internal governance of the cooperatives is also provided.

Market shares of cooperatives differ substantially across sectors and countries. Figure 4.1 presents the share for the EU as a whole, per sector, and for all sector together (weighted for the relative importance of the sector in total EU agriculture). Cooperatives are most important in dairy. Other sectors with an important role for cooperatives are olives, wine, cereals, and F&V. For the EU as a whole, cooperatives take care of about 40% of agricultural products at farm gate value (excluding products they buy as an IOF in other countries).¹⁴ In the following sections we will discuss details of cooperative presence in each of the eight sectors.

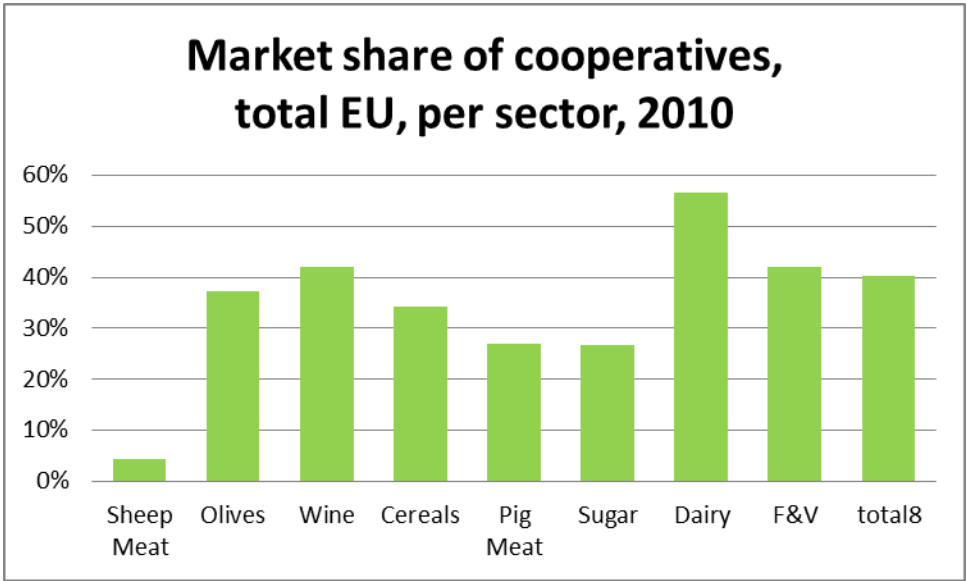


Figure 4.1. Market share of cooperatives, per sector and total EU, 2010

In discussing cooperatives' position in the food chain, attention will be paid to their growth strategies and branding activities. Four different options for growth strategies were identified: autonomous growth, horizontal mergers, vertical mergers & acquisitions, and international mergers and acquisitions. According to our fact finding, growth strategies in all sectors rely to a high degree on autonomous growth (increasing turnover by extending the current market and selling more or attracting new members). Given the concentration process in the cooperative sector in many countries in Europe it was expected that the common way of growth was mergers (with neighbouring cooperatives) and not autonomous growth. This finding came as a surprise to us, particularly given that, historically, most large cooperatives have been the result of several mergers of smaller and/or inefficient cooperatives. One possible explanation is that

¹⁴ See also note 12 on the calculation of this figure for the EU as a whole

the cooperative leaders interviewed for this study were reluctant to reveal their intention to acquire neighbouring activities. For the cereals and dairy sectors horizontal M&As represent the second most important strategy. Vertical and international mergers and acquisitions explain cooperatives' growth only to a minor extend.

An analysis of the range of branding activities performed by cooperatives shows sector-specific differences. In the wine sector cooperatives' turnover is basically the result of sales of branded products. In this sector the establishment of own brands has a long tradition and it is in the focus of most cooperatives. Dairy cooperatives also invest in and promote their own brands, but there are still a larger number of cooperatives with a smaller proportion of branding activities. In both sectors cooperatives are part of the final market where the supply of their own branded products and the ability to produce private label products is a requirement. Sector-specific characteristics explain the low degree of branding activities in the cereals, sugar, sheep and pig meat sectors.

4.2 Dairy

Marketing cooperatives in the dairy sector are strong competitors on the markets. Dairy cooperatives are active in almost every part of the food supply chain. They are collecting and processing the milk delivered by their members, they are producing branded products or private label products and are selling these directly to retailers. Although the three biggest companies in the dairy sector are IOFs (Nestle, Danone, Lactalis), the next four are cooperatives (FrieslandCampina, Arla Foods, DMK, Sodiaal). There are several transnational and international dairy cooperatives active.

Dairy cooperatives in Europe perform quite well. In thirteen EU-countries they have a share of more than 50% of the market (measured in milk volume collected at the first-handling and processing stages). Exceptions are found with some smaller producers (Portugal, Malta, and Slovakia). In the Scandinavian countries (Sweden, Denmark, Finland) and in Ireland and Austria market shares exceed the 90%-level (Figure 4.2).¹⁵ The average share of cooperatives¹⁶ in the EU dairy industry is 57%. The market share of cooperatives in a region is an important determinant of the regional milk price (see Chapter 6 for the analysis).

The organisation of farmers in cooperatives is explained by both the product attributes of milk and the constantly fluctuating markets for agricultural products. The production of fresh milk requires significant investments in infrastructure, equipment, and the development of relevant skills. Such investments are characterised by a high degree of asset specificity thus making milk producers vulnerable to ex post opportunistic behaviour by dairy processors. In order to protect their investments, farmers organise dairy cooperatives that enable them to access dairy markets. Further, the fresh milk is highly perishable, vulnerable to quality differentials and malpractices that jeopardise hygiene, and comparatively heavy commodity, farmers benefit from collective investments in transportation, processing, and quality control. Historically, the formation of dairy cooperatives accelerated during the era that cheese and butter production moved from the farms to factories in order to achieve the scale efficiencies afforded by the steam and diesel engines. Although individual entrepreneurs were active in these markets, they have been out-competed by cooperatives due to the above mentioned reasons.

In almost all EU Member States, the cooperative market share has increased in the decade 2000–2010. Almost half of the dairy cooperatives also supply inputs to their members (especially in Ireland, France, Portugal, and the Czech Republic). About 20% of the dairies also supply credit to their members. More than 25% of the cooperatives are also producers of milk (e.g., in Estonia, Spain, Slovakia and Romania). In most western and northern regions of Europe production is organised on private farms while dairies focus on processing and marketing.

Obviously, many dairies could not be classified into a single strategy. Most dairies (~65%)

¹⁵ The exact figures are presented in Table 4.1 at the end of this chapter.

¹⁶ Weighted by national milk sales at the farm level

follow a differentiation strategy and a little more than 40% follow cost leadership and focus strategies. To sum up, Western European cooperatives often pursue differentiation strategies, whereas in most New Member States cost leadership dominates as a generic strategy. All of the larger dairy cooperatives in our sample have plans to grow by mergers and acquisitions.

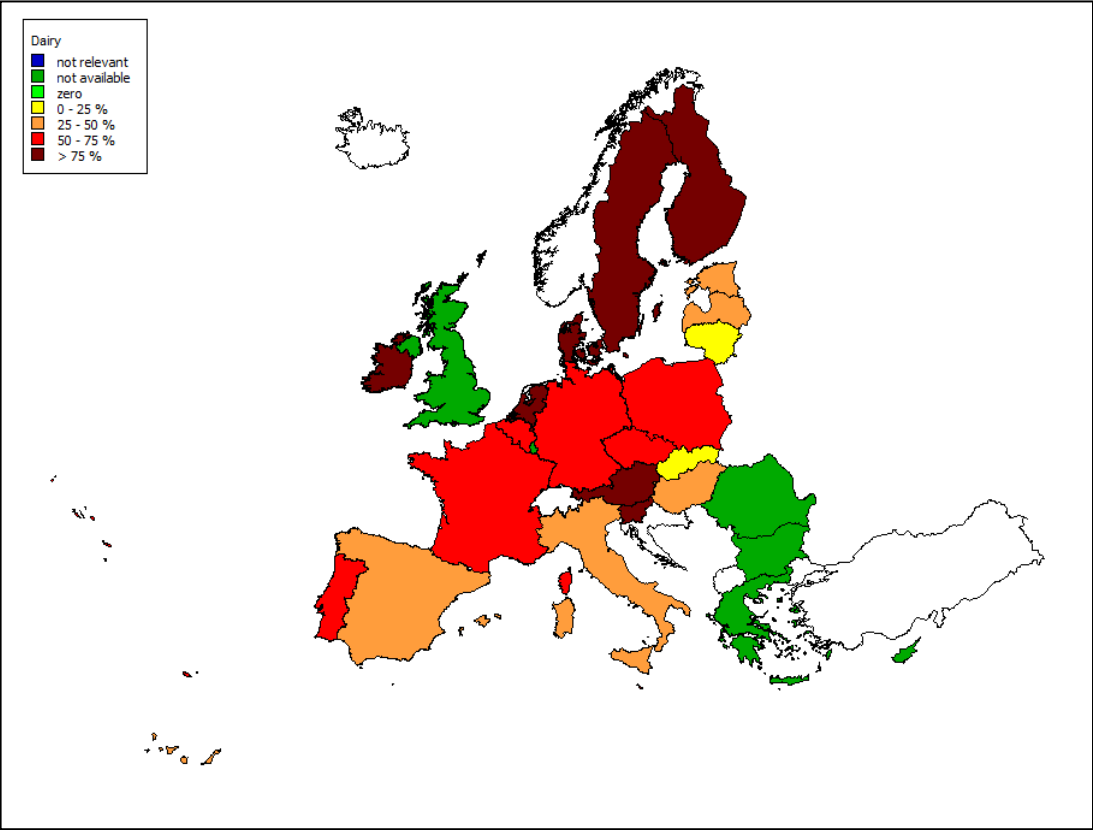


Figure 4.2. Market share of dairy cooperatives, 2010

As one would expect, the larger the cooperative (measured by turnover) the more likely it is that professional managers serve on the board of directors. In the lower half of the distribution only 8% of the dairies have professionals serving on their boards; in the upper half these figures increase to 26%. More often than in other sectors, cooperatives are organised in holding structures. Another structural peculiarity worth to note, is that about a fifth of the cooperatives use product groupings. Large dairies make use of this mechanism more often. Large cooperatives with a diverse product portfolio, may want to make sure that members are represented in interest groups according to specialized products. More than any other sector, dairies make use of subsidiaries. About a quarter of the dairies have subsidiaries, as compared to only 7–14 per cent for cooperatives in other sectors. For the upper half of the dairies (by turnover) these figures go up to more than 30%. Compared to other sectors, dairy cooperatives and their members maintain closer ties, as reflected in the smaller openness to non-members and the relatively high shares of dairies who do not engage in trade with non-members.

Almost 60% of the large cooperatives pay volume premiums, compared to less than 20% of the small. Larger cooperatives are also more likely to apply differentiated cost policies, supposedly because they have a larger product portfolio and therefore demand more differentiated milk qualities.

Policy measures affecting the dairy sector are numerous and sometimes country-specific. No single policy measure of the ones identified in the country studies can be solely made responsible for successes or failures of cooperatives. Quotas, as part of the institutional environment of dairy production, have been very influential. The end of the quota system in 2015 may make it necessary for dairy cooperatives to design contract stipulations similar to

delivery rights applied by IOFs. Another option is to refrain from an open membership policy in order to control production levels. Both alternatives deviate from traditional cooperative principles.

In late 2010, the EC “milk package” proposal was drafted. Since then, aspects of contractual relations between farmers and dairies, the EU-wide promotion of bargaining producer organisations and limits of firm concentration on the basis of national market (33%) shares or market shares in the EU (3,5%) were discussed in order to level the playing field between producers and processors. In this debate, the role of existing cooperatives has been sometimes praised and sometimes questioned. However, regulators’ size restraints for mergers in the dairy market (milk package) have to be considered with great caution. Even more important with regard to cooperative development seem to be measures which assure that in the speedy process of mergers the owners of the cooperative understand objectives and dangers and can play their roles in supervision and control.

4.3 Pig meat

The European pig meat market is very integrated, partly due to the fact that it is very closely linked to global markets and thus affected by their structure and performance. The production of pig meat in EU is approximately 10% higher than consumption. The largest exporting countries are Germany, Denmark, the Netherlands and Belgium. The main export markets are in Asia where competitors include the US, Canada and Brazil, countries that, in general, have lower production costs.

Due to the price volatility and sensitivity that characterise production, one might think that producers were eager to organise themselves into cooperatives. However, compared to, e.g., the dairy and fruit and vegetable sectors, the market shares of cooperatives in the pig meat sector are in general much lower. There are also different kinds of cooperatives in EU. In Northern Europe, cooperatives are usually large, and in addition to collecting the carcasses, they slaughter and process them into consumer products (incl. convenience food). In Southern Europe, in addition to these large cooperatives, there exist a number of small cooperatives that only sell live animals to small local slaughterhouses and butcher’s.

There are only five countries where the cooperatives’ role in this sector is dominant: Denmark (Danish Crown), Finland, Sweden (due to the transnational role of HKScan), Malta and France. Further, VION, a company owned and controlled by a farmer organisation is a key player in the Dutch and German pig meat industry. Of the other countries only in Belgium, Czech Republic, Germany, Hungary, Spain, Austria and Italy the cooperatives have important shares (Figure 4.3). In many Eastern European countries the role of international companies and cooperatives is already now quite important (e.g. HKScan in Poland).

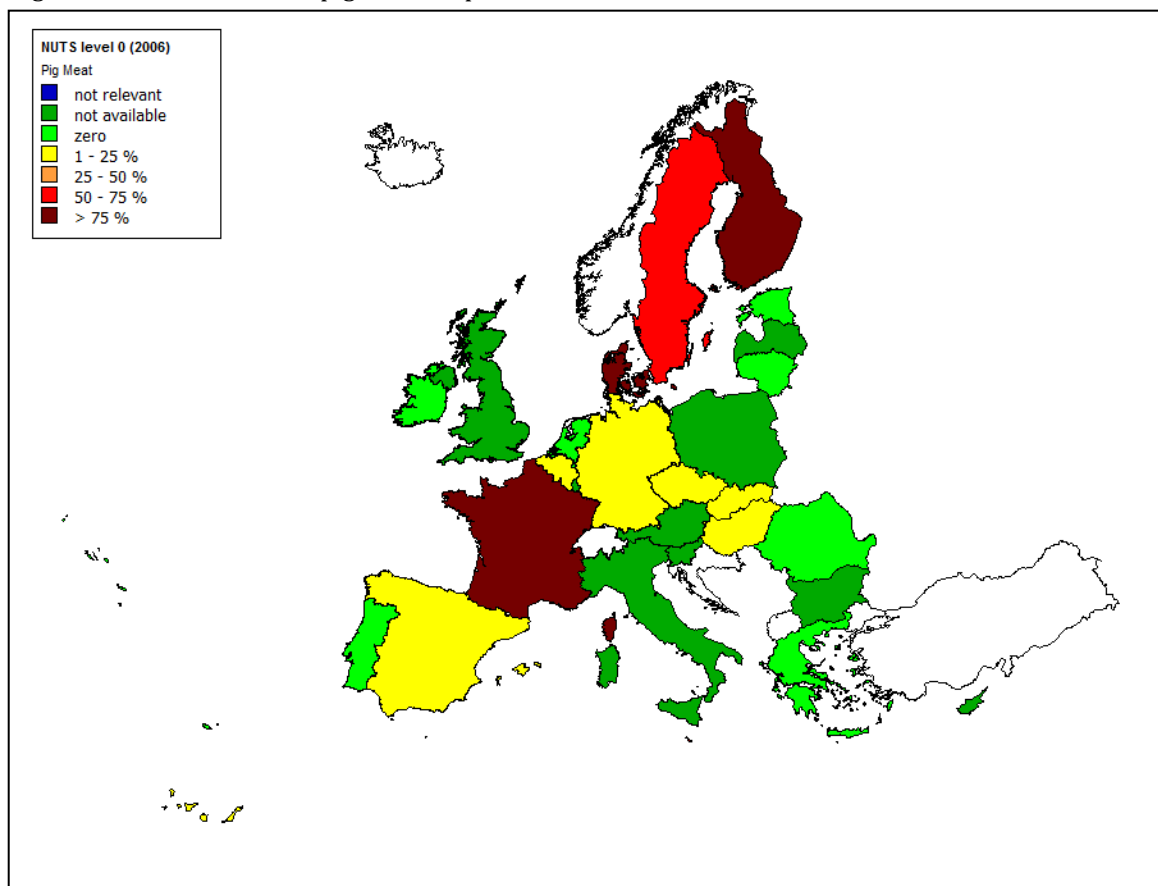
Cooperatives in the pig meat sector are serving nearly every stage of the food chain, from transport and storage, to primary and secondary processing, marketing of branded products, wholesaling and retailing. In Eastern Europe there are cooperatives that have an important role in primary production. Cost leadership is important, branding much less – which confirms the commodity character of pig meat.

In addition to retained surplus, 30% of the cooperatives require a substantial equity contribution from members. Seventy per cent of the cooperatives have only an entrance fee, which may vary in size and in some cases may be connected to the use of cooperative services.

More than half of the cooperatives also trade with non-members. In contrast to the dairy and F&V sectors, non-member transactions are very significant. There are many cooperatives that cover supply by non-members at a percentage of 10-50%.

The cooperative organisational form does not seem to be an obstacle in being competitive (although we could not prove with an econometric test that it helps, like in dairy). Neither does it give any special advantage, especially not in the second processing stage. This is also implied by the concurrent existence of various federated or hybrid cooperative structures. Such models may be adopted more often in the future, following the examples of the stock market listed HKScan and Atria, or VION.

Figure 4.3. Market share of pig meat cooperatives, 2010



There exist significant differences between countries in terms of the cooperatives' performance in the sector. However, the legislation and regulation concerning cooperatives do not differ that much. Although many policy measures (including environmental, animal welfare and disease control legislation) are relevant, it seldom has specific consequences for cooperatives compared to IOFs. Thus, one can conclude that there are no specific policy measures that could be interpreted to foster more the role of cooperatives in one country compared to another country. It seems that, overall, the observed differences in cooperative market shares might be explained by relevance to the historic evolution of cooperatives and related path dependencies.

4.4 Sheep meat

Sheep meat production is concentrated in a limited number of countries or even regions. In general, the heterogeneity in farm size is great, even in specialised farms. For example, in Spain the production is very dispersed, from many small operations to farms with thousands of heads of stock. Many farms that have some sheep are specialised in other products (like cattle), in nearly all countries less than 10% of the animals are raised in specialised farms. This farm heterogeneity may inhibit the organisation of farmers into sheep meat marketing cooperatives.

In countries where the sheep meat sector is of little importance, sale of sheep meat is mostly done through direct sales in the local market. For example in the Czech Republic and Slovenia most of the consumption is covered by household slaughtering (home slaughters). Between 35-45% of the lamb and other meat in Bulgaria is produced in farms and used for local consumption. Consumers prefer such market channels because of lower prices and because they trust farmers whom they know personally. It has also been suggested that in several countries such direct sales might also be attractive from the point of view of tax (evasion). Historically this

has been relevant for farm sales in many countries, but with the EU wide introduction of the registration of goats and sheep by ear tags, in principle tax authorities have an extra monitoring mechanism.

In most countries the cooperative sector is not well developed as far as production and processing is concerned. Where cooperatives exist, their position in the food supply chain is rather weak (with market shares of 20% in the Czech Republic, 25% in Spain, and 20% in Hungary), except in Sweden where cooperatives have a market share of 55% (Figure 4.4).

The three largest sheep cooperatives are all based in the UK (Fane Valley, ANM Group, Yorkshire Farmers Livestock Marketing), followed by two Spanish ones (Carnes Oviaragón and Oviso). The two largest cooperatives have also important activities in dairy, feed, other types of meat, energy and more). This shows that sheep cooperatives are primarily located in less favoured areas (Scotland, Ireland, Yorkshire, Extremadura, and Aragon). These regions are characterised by a high degree of specialisation in sheep meat and big herds and a great distance to the market. In these isolated regions markets had to be created, transport organised and farmers depended on only a few information sources to find out prices in the distant market. As a result, auctions, cooperative trading companies or cooperative slaughterhouse became attractive options.

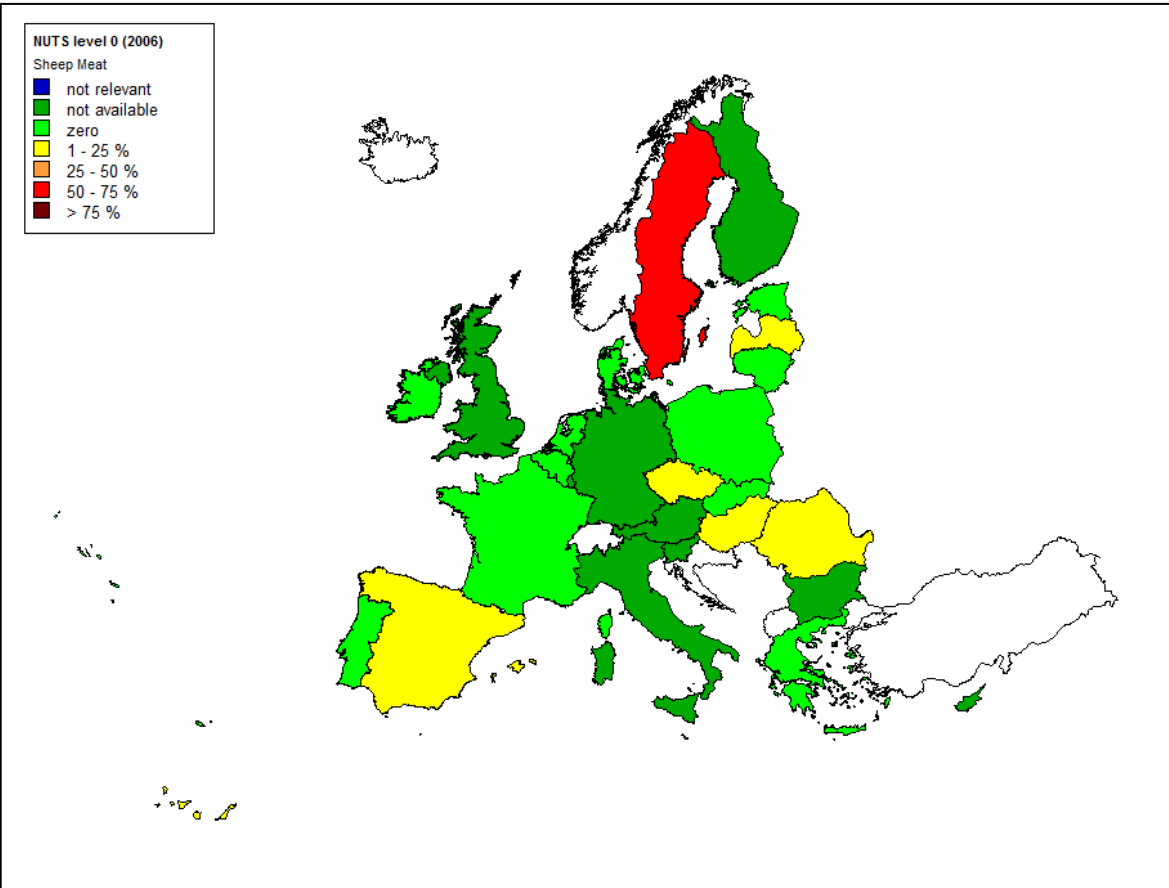


Figure 4.4. Market share of sheep meat cooperatives, 2010

The main functions of cooperatives are close to farming and consist of collecting members' products, wholesaling, and the provision of some technical assistance. Marketing of branded products is as rare as secondary processing, although there are interesting exceptions like the federated cooperative Oviso in Extremadura that commercialises its lamb carcasses in the national and the EU market under its own two brands: CORDEHESA and CORSERENA.

The last CAP Reform in 2003, by introducing the decoupling of direct payments, accelerated the contraction of the sheep sector. However, it has also brought professionalization and dynamic changes, as one of our case studies suggests. There are not many (national) support

measures for sheep cooperatives. In Spain, many cooperatives increased the number of members due to the fact that the concentration of supply resulted in more price stability and a stronger presence in the market. It seems that a national policy measure that provided subsidies for improving the production of quality agro-food animal products has had a positive effect.

4.5 Wine

The European Union is the leading producer, consumer and trader of wine globally. Over the past ten years, the European wine industry is in turmoil due to globalisation and new marketing methods. The European wine industry is structured around three types of business organisations: large international multi-beverage firms, large specialised wine-making companies, and small and medium-sized wineries that are involved in both production and sales.

Wine cooperatives buy grapes from their members and produce wine which is sold either bottled or in bulk. This diversity of business models reflects the degree of fragmentation of the wine supply chain throughout Europe. Although there are several vertically integrated wine cooperatives that market and sell their wines both in domestic and international markets, the competitive position of cooperatives in the sector is rather weak. There is a so-called dual structure: on the one hand there is a group of dynamic market oriented cooperatives that have managed to deal with market changes and strong branding and marketing activities. On the other hand, there are many cooperatives that are dedicated to only collecting grapes or bargaining prices.

Wine cooperatives in Spain have a cumulative market share that reaches almost 70% (Figure 4.5), the highest in Europe. However, the commercialisation of products from cooperative wineries continues to be quite insignificant compared to the industry in general and represents one of the main problems of cooperative wineries. A high percentage of wine sold in bulk is no guarantee for success if cooperatives do not dominate the (branded product) market. Among the rest of the wine producing countries, cooperatives hold significant market shares in Austria, France, Germany, Italy, Malta, Slovenia and Portugal.

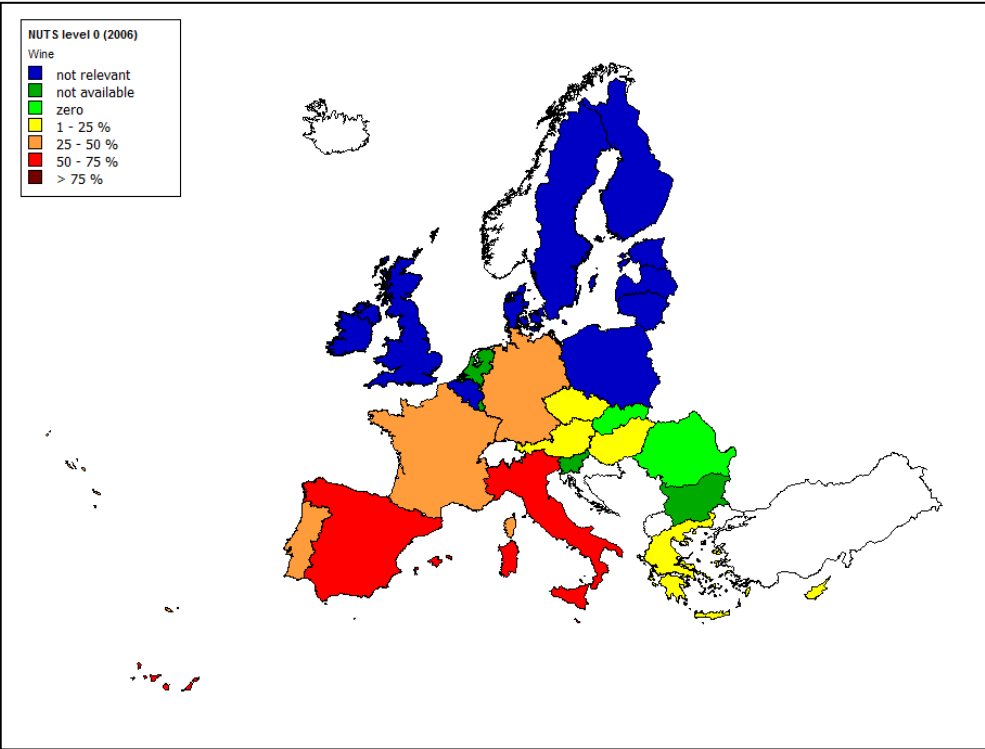


Figure 4.5. Market share of wine cooperatives, 2010

Wine cooperatives often act as the “last resort buyer”. In other words, members sell their top quality grapes to investor-owned wineries and supply the cooperative with whatever is left. This practice leads to low quality wines that suffer in the market place and ruins the cooperative’s brand name. Usually, wine cooperatives buy grapes from their members at market prices. Then the surpluses, if any, are distributed to members according to patronage. Implementing strict quantity and quality rules (e.g., requiring that members bring all their production to the cooperative) and providing members with the right incentives to adhere to these rules are critical for the survival of cooperative wineries. In case a cooperative markets very high-quality, aged wines, still it pays its members the regular market price for the grapes they deliver. When the cooperative sells the produced wine at a premium price (sometimes many years after the grapes were harvested), the generated surpluses and/or profits are distributed to current members in proportion to patronage. As a result, the cooperatives suffer from the so-called internal free rider problem.

Despite their significant market shares, wine cooperatives in most EU countries suffer from fragmentation. Many small cooperatives serving local or niche markets is a typical phenomenon in Europe. The significant amounts of risk capital required in order to invest in the high value-added segments of the wine supply chain might explain the reluctance of farmer cooperatives to engage in such segments. Grape growing farms show a negative net investment in the majority of the EU’s wine-producing countries as well.

In some countries, the observed difficulty of cooperatives to either increase their market shares autonomously or merge with other cooperatives is explained by the fact that wine producing regions are close to consumption centres thus enabling direct marketing of wine to consumers by farmers (e.g., Austria).

While most of the top-5 wine cooperatives in France, Italy, and Germany view marketing branded wine as their major goal, only one out of the five Spanish cooperatives engages in selling branded wine. At the same time, European wine cooperatives are very active in selling wine in bulk; even those that focus on high quality, branded wine, they also make a part of their sales in bulk wine. Nevertheless, in terms of their total turnover, the top-5 wine cooperatives in all major wine producing countries of the EU have improved their competitive position since 2000. In some of these countries the improvement has been considerable.

In all top-5 wine cooperatives in the main wine producing countries of the EU (France, Italy, Spain, Germany, and Portugal), members sign marketing agreements with their cooperatives. These agreements are contracts that legally bind farmers to their cooperative; members are obliged to deliver their produce to the cooperative. The cooperative or an independent company, in some cases, assesses the quality of grapes and producer-members are paid accordingly.

The top-5 wine cooperatives in France and Spain have assigned the operational management to professional managers. On the other hand, in Portugal and in four of the top-5 cooperatives of Italy the board of directors is responsible for day-to-day operational management. In Germany the situation is mixed.

In Italy and Portugal there is no Supervisory Board in any of the top-5 cooperatives. On the other hand, in each of the top-5 cooperatives in Germany there is a Supervisory Committee. In terms of the rules adopted in voting for members of the board of directors, the personal expertise of candidates is of utmost importance in Germany and Portugal while regional representation is the most important criterion in France. In Spain, both criteria are taken into account. The voting rule implemented by most wine cooperatives is the one-member, one-vote rule. In the few French and Spanish cases where proportional voting is allowed, the volume of member transactions is used as the sole criterion in allocating proportional voting rights.

Wine cooperatives have benefitted from the CAP, through several supporting measures. These measures provide cooperatives with the financial leverage needed to invest in infrastructure and the improvement of wine-making equipment in order to produce and distribute quality wine. Moreover, the Common Market Organization (CMO) includes an aid scheme for promotion of wines in third countries and several cooperative wineries have been involved in it. This measure allows cooperatives to penetrate export markets, and establish a successful brand name.

Additionally, wine cooperatives have been indirectly affected by the 2008 reform of the CMO. This reform intended to ensure that production meets demand and to eliminate overproduction, in order to enhance the competitiveness of European wines in the world market. An important aspect of the new CMO is that a “National Envelope” has been allocated to each Member State in order to create individual support plans that better fit the particularities of each country. Another important policy scheme is the “grubbing-up”. However, it is bound to attract relatively low yield areas that produce low price/ low quality wines.

Wine cooperatives have benefitted from EU promotion measures in order to increase their market share. In most EU countries, wine cooperatives have come a long way since their formation in the late 19th and early 20th centuries. Given the international trends in the production and consumption of wine, among which the competition from inexpensive New World wines is probably the most important, European wine co-operatives need to invest in brand recognition and, more generally, in downstream parts of the wine supply chain. The EU measure of promotion of wines on third country markets precisely targets in this direction. Beneficiaries of the third countries promotion program tend to improve their ability to serve their members from a stronger competitive position.

Under this measure, 464 programs in more than 30 countries have been approved with an investment of € 160 million. In 2011, 760 programs and an investment of 84 million Euros was expected. Even though the cooperatives’ involvement in promotion programs varies across Member States, there are, undoubtedly, strong positive effects. This measure allowed cooperatives to penetrate export markets and to establish a successful brand name. However, the quantification of the positive effects of promotion program for wine cooperatives is not an easy task, mainly because the results are usually realized in the long-run.

4.6 Olive oil and table olives

Olive oil is a typical product of the Mediterranean basin, where more than 90% of the global production takes place. After olive oil is extracted, if the mill is owned by a farmers’ cooperative, the olive oil is stored in tanks maintained by the cooperative. Members can either agree to sell this olive oil in bulk collectively or individually. Unless the cooperative bottles and sells branded olive oil, usually marketing channels are only vaguely known in advance.

The quality of olive oil depends on some crucial parameters such as the location of the farm, the particular olive variety planted, the quality of soil, weather, the production methods adopted, the olive oil extraction technology used, the quality of the tank and length of storage, etc. Farmers through the farming techniques adopted can improve the quality of olive oil significantly. This is why during the last ten years many cooperatives have adopted various integrated production systems and protocols; members sign contracts with the cooperative that penalise those who do not follow the instructions of certified agronomists.

The olive oil supply chain is characterised by a low degree of cooperative mill-initiated vertical integration into other downstream activities (e.g., bottling). Cooperative-owned mills may sell olive oil to farmers and other local customers for home consumption. Also, they sell in bulk to refineries, packing plants and merchants.

The position of cooperatives in the olive oil producing countries is different. In Italy the cooperatives were not able to create significant added value to the product and, consequently, their market share dropped (from 13% in 2000 to 5% in 2010). Spanish cooperatives still have the highest market shares (70%) but, as well as in Italy and Portugal (from 35% in 2000 to 30% in 2010) they are losing market share. Greek numbers for 2010 are not available, but in 2000 cooperatives’ market share was 60% (Figure 4.6). Also the largest olive oil cooperatives are Spanish (Hojiblanca, Agro Sevilla Aceitunas, Jaencoop, and Oleoestepa) followed by an Italian (Oleificio Montalbano) and a Greek cooperative (U.A.C. of Heraclion). The larger size of Spanish cooperatives might be influenced by the fact that the Spanish retail system is much more characterised by big retail chains.

In most cases, cooperatives and producer groups sell olive oil in bulk to IOFs which bottle and brand it in order to capture the high value added through these activities. The significant

amounts of risk capital required in order to invest in the high value-added segments of the olive oil supply chain might explain the reluctance of farmer cooperatives to engage in such segments. Olive farms show a negative net investment in the majority of EU olive oil producing countries as well as very low average farm net income.

Only Portuguese olive oil cooperatives focus exclusively on providing marketing (processing) services to their members. In all other countries, cooperatives also provide their members with farm supplies and/or various other services. European cooperatives have a strong position in the processing functions that follow the first-handling stage within the olive oil supply chain.

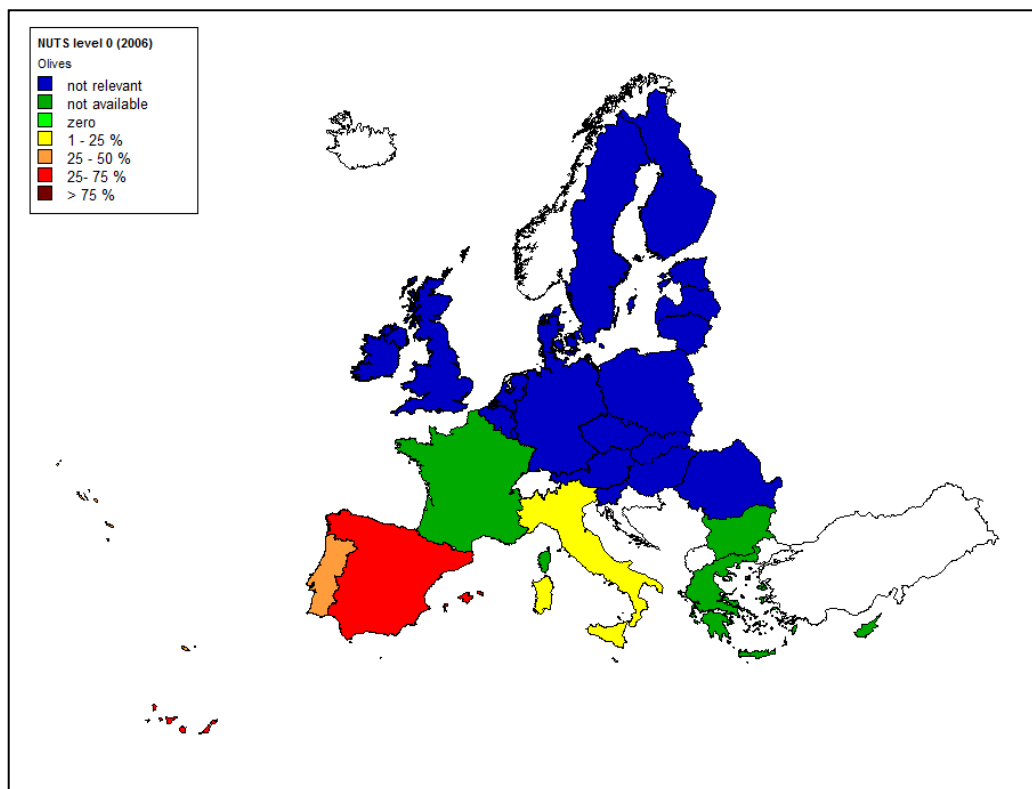


Figure 4.6. Market share of olive cooperatives, 2010

Among the Spanish top-5 olive oil cooperatives, operational management is in the hands of professional managers at least in three cases. Similar is the situation in Greece, although chairpersons have a significant influence even on day-to-day operational decisions. On the other hand, in the top-5 cooperatives in Italy and Portugal the operational management is implemented by the Board of Directors. Regarding the rules that apply to the election of members on the board, regional representation is the basic criterion used in Greece where the olive oil and table olives cooperatives are second-tier organisations whose members are primary cooperatives. Personal expertise is the most important criterion used in Italy and Portugal while no specific rule is applied in Spain.

The federated cooperative structure where local, first-tier cooperatives collect the olives from members' farms and then forward them to the second-tier cooperative in order to extract olive oil, bottle and brand it (or sell it in bulk) seems to have reached its limits at least in some countries. While in past times the road network and transportation technologies posed significant constraints to what and how fast could be transferred from farms to processing facilities, 21st century conditions make some of the coordination schemes of the past obsolete.

The cooperatives have benefitted from the CAP in terms of support received for investment and professionalization. In this sense, olive oil cooperatives have received funds to build or modernise olive oil mills, and invest in new facilities and equipment. Moreover, CAP has

subsidised investments in quality-guaranteeing systems. These systems allow cooperatives to adopt various integrated production systems and protocols; members sign contracts with the co-operative that penalize those who do not follow the instructions of certified agronomists. Finally, olive oil co-operatives have been subsidised for carrying out promotion activities. The abovementioned support measures provided the financial leverage to cooperatives to improve their economic situation and competitive positioning in world markets. However, the efficiency of these policies differs among cases.

Apart from the above measures, the CAP has indirectly affected the olive oil cooperatives by several market-based and structural aid policies that have, in general, benefitted the sector. In the market regime, production and consumption aid, price support and trade barriers to third countries are the main identified instruments. On the other hand, the structural aid policies aimed at enhancing productivity, via the restructuring of the orchards and infrastructure improvements. In 2004, however, the olive oil sector has been integrated into the single farm payment scheme and production-based subsidies were abolished. Under this new scheme, “cross compliance” has become obligatory. This reform is expected to lead, in the long-run, to a reduction in EU production of olive oil and a simultaneous improvement in its quality.

4.7 Fruit and vegetables

The fruit & vegetables (hereafter: F&V) sector consists of a large number of different products. The most important vegetables, in terms of volume harvested are tomatoes, carrots and onions. In the category fruits, the main products are apples, oranges and pears. F&V are characterised by being perishable and seasonal, but also by the variation in quantity and quality (due to natural conditions). Substitution between these products exists, as well as between the different forms in which F&V are offered to consumers: fresh, canned, frozen or dried, pre-packed or ready-to-use.

The perishability has implications for the organisation of sales and distribution: efficient logistics is critical and the seller is more vulnerable to opportunistic buyer behaviour after a contract (with future delivery) has been agreed. As a consequence of these and other characteristics, the F&V marketing system represents a complex and diversified organisational structure.

Cooperatives in the fruit and vegetable (F&V) sector cover the whole range of different functions with the most important being the provision of a market to their members, the collection and marketing of farm products and also, secondary processing. Cooperatives in three countries (The Netherlands, 95%; Belgium, 83%; Denmark, 70%, and Slovenia 68%) have a comparable high market share (Figure 4.7). The largest cooperatives are Dutch (Coforta/The Greenery, FresQ), Italian (Conserve Italia), German (Landgard) and Spanish (Anecoop). It is remarkable, that given the country’s large fruit and vegetable sector, French cooperatives are relatively small, with one cooperative just in the top-10 (Sica St. Pol, one fifth the size of the Greenery) and three others completing the bottom of the top-20.

Over the years 2000-2010, market shares of cooperatives in the F&V sector have increased. The Netherlands and Belgium clearly stand out with their high market share, mainly due to two factors. One is the history of F&V cooperatives in those two countries. Traditionally, F&V marketing in these countries has been dominated by cooperative auctions. In Belgium, most of F&V continue to be sold through cooperative auctions, while the auction as a price determination mechanism has been almost abolished in The Netherlands.

In other countries where the F&V sector is an important part of agriculture, particularly the Mediterranean countries, cooperatives have a substantial market share in Italy and Spain (both around 50%), but in France, also a major producer, the market share is only about 35%. In Germany, which is important particularly for apples and onions, the market share of cooperatives is about 40%. In Poland, also an important producer of apples and onions, the market share of cooperatives is about 11%. However, this could be low due to underreporting as many farmers are marketing their produce through a producer group that does not adopt the legal form of cooperative (Banaszak, 2008a).

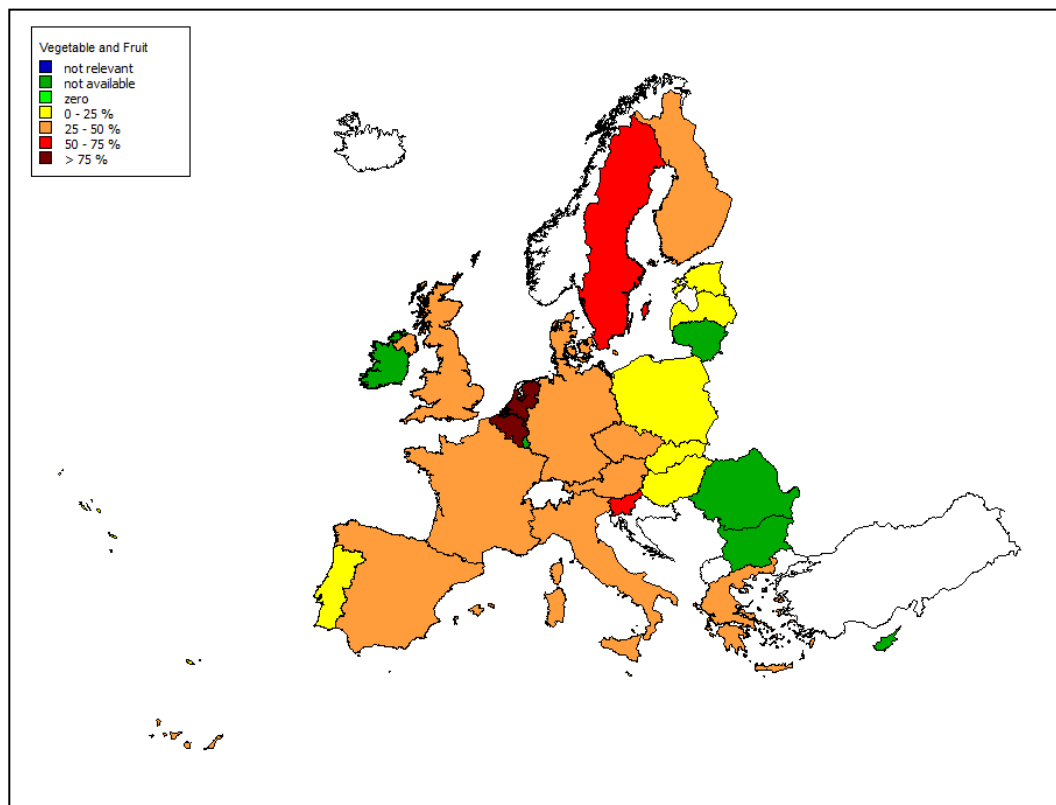


Figure 4.7. Market share of fruit and vegetables cooperatives, 2010

There are several transnational cooperatives but, they mainly cross borders between the Netherlands and Belgium, and sometimes with Germany or the UK. An exception is FINAF, which brings together Italian and French fruit growers. There are also quite a number of international cooperatives.

One important type of F&V cooperative is the grower-owned cooperative auction, which has a number of advantages for its members. First, growers can fully specialise in production, as the marketing of their products is taken care of by the cooperative (over which they have joint control). Second, auctions provide transparent markets. Growers know exactly what prices they and their colleagues have received for their products. Sales transactions are a rather simple transaction, without additional conditions. This transparency reduces transaction costs for growers. However, auctions only work well under certain conditions. There has to be sufficient demand, preferably more demand than supply. If not, the transparent market of an auction leads to very low prices. Second, there needs to be sufficient buyers present at the actual time of selling. Third, logistics has to be organised well, for speedy delivery of products to and rapid distribution from the auction facilities.

Despite their advantages for growers, most of the F&V auctions in the Netherlands have been transformed into marketing cooperatives that mainly work with bilateral contract negotiations (Bijman and Hendrikse, 2003). The main reason to abolish the auction clock was the threat of major retailers buying their products elsewhere. Retailers, and particularly the large ones, do not like auctions as they prefer to plan their purchases and their promotions long in advance (which is not possible on a spot market like the auction). Also, retailers want to buy large quantities of uniform products, which is not easy in an auction. But also an increasing number of growers had become unsatisfied with the auction system, as innovation and direct contact with customers was discouraged.

Another interesting type of cooperative in the F&V sector is the bargaining association or cooperative that does not own assets (and often not even the product) but negotiates with buyers like the processing industry (see Chapter 6 for a special analysis on this type of cooperative).

Activities downstream in the food chain have become more relevant in the last decade: more cooperatives are carrying out processing, wholesaling, and retailing activities. Also, the marketing of branded products has become more important.

Out of the 105 F&V cooperatives in our sample, a slight majority has professional managers taking care of operational management. This is more often the case in the North-West European countries. Some cooperatives have both a Board of Directors and a Supervisory Committee, the latter having a control function towards the Board of Directors. There is an interesting difference between the North-Western and the Mediterranean countries: in the Mediterranean countries almost all F&V cooperatives have only a Board of Directors (and no Supervisory Committee), where in the countries of the North-West, 44% do have a supervisory committee. Only 11% of the F&V cooperatives in our sample (where the smallest coops are not represented) have non-members incorporated in the Board of Directors. Boards with outside experts can only be found in the North-West and the East of the EU. None of the Mediterranean countries have outside experts serving on the board.

Producer Organisations (POs) have been an important element of EU policies in the F&V sector. This is the main piece of EU and national legislation that directly impacts cooperatives and producer organisations in the F&V sector, consisting of several EU regulations. In most of the Member States the European policy on POs in the F&V sector has been effective although a handful MS have not yet succeeded in setting up producer organisations. Already in 1972, POs were defined in EU legislation as any organisation of fruit and vegetable producers which is established on the producers' own initiative for purposes such as promoting concentration of supply and the regularisation of prices at the producer stage of the food chain and making suitable technical means available to producer members for presenting and marketing the relevant products. Since 1972, the Common Market Organisation (CMO) for F&V has undergone various reforms and has been included in the Single Payment Scheme of the CAP. The regulation states that POs are legal entities recognised by the Member State and set up on the initiative of producers. Minimum recognition requirements are set, particularly as regards the number of members and turnover. Member States, however, have some freedom in using additional requirements as to the minimum number of members or the legal form. POs oblige their members to sell their total output through the organisation (i.e., concerning the product(s) for which they have become members of a PO). Also, members need to comply, with regard to production and marketing rules which have been adopted by the PO with a view of improving product quality and adapting the volume of supply to market requirements. The CMO encourages POs to have a multi-annual operational program, which is co-financed by producers and the Commission. The EU legislation on POs seems to have reinforced the competitive position of cooperatives.

4.8 Sugar

Sugar beet is a root crop, and a rotation crop, grown on farms in combination with other crops, e.g., cereals, oil seeds, potatoes, etc. The harvested sugar beets are transported to the plants (factories) immediately or in some days after the harvest. The harvest and processing campaign between September and January is a large logistic optimisation process. The farmer wants to harvest as late as possible (but before frost sets in) in order to reach as high yield and sugar content as possible. But the sugar beet processing plant needs a regular supply of sugar beets to keep the process going and optimise capacity use. This means that the sugar beet is not a tradable product for farmers like, for instance, cereals or ware potatoes. The farmer needs to have a destination (a factory) for the sugar beet in advance, either by contract with an IOF or with his cooperative.

Due to the reform of the sugar policy, several countries gave up sugar production. In most countries the producer-owned sugar refineries seem to have a strong position and they cover nearly every function in the food supply chain. Having or not having a cooperative sugar industry seems to be determined by history. Cooperatives are strong in processing and also in marketing of branded products. For the Netherlands (100%), France (62%), Hungary (30%),

and Spain (28%) cooperatives play an important role. In Germany the situation is rather ambiguous as the two main companies, SüdZucker and NordZucker, have a federated and hybrid character; officially they are an IOF, but sugar beet farmers own shares of the company.¹⁷ They are partly farmer-owned (Südzucker is even majority farmer-owned), but they are not necessarily user-owned (which is one of the three elements of our definition of a cooperative). Südzucker is also linked with the Austrian Agrana (see Chapter 6 for more details). These German companies, French Tereos and Dutch Cosun are among the five largest European sugar producers, together with the British IOF British Sugar. The cooperatives are internationally oriented, with suppliers and sometimes members in other countries. They are also active in other products, sometimes linked to the activities of their members; potatoes, vegetables or bio-energy crops.

The Western European cooperatives all are large organisations; the average number of members is 7,000 and turnover is counted in billions. Processing and marketing is their most important activity, while only a few cooperatives provide other services to their members, besides advisory. While access to the cooperatives is often restricted, the cooperatives also process sugar beets from non-members. The management is professional. The Board of Directors is formed by members, sometimes complemented by professionals. The operational management consists of only professionals. Members are obliged to deliver their sugar beets to the cooperative.

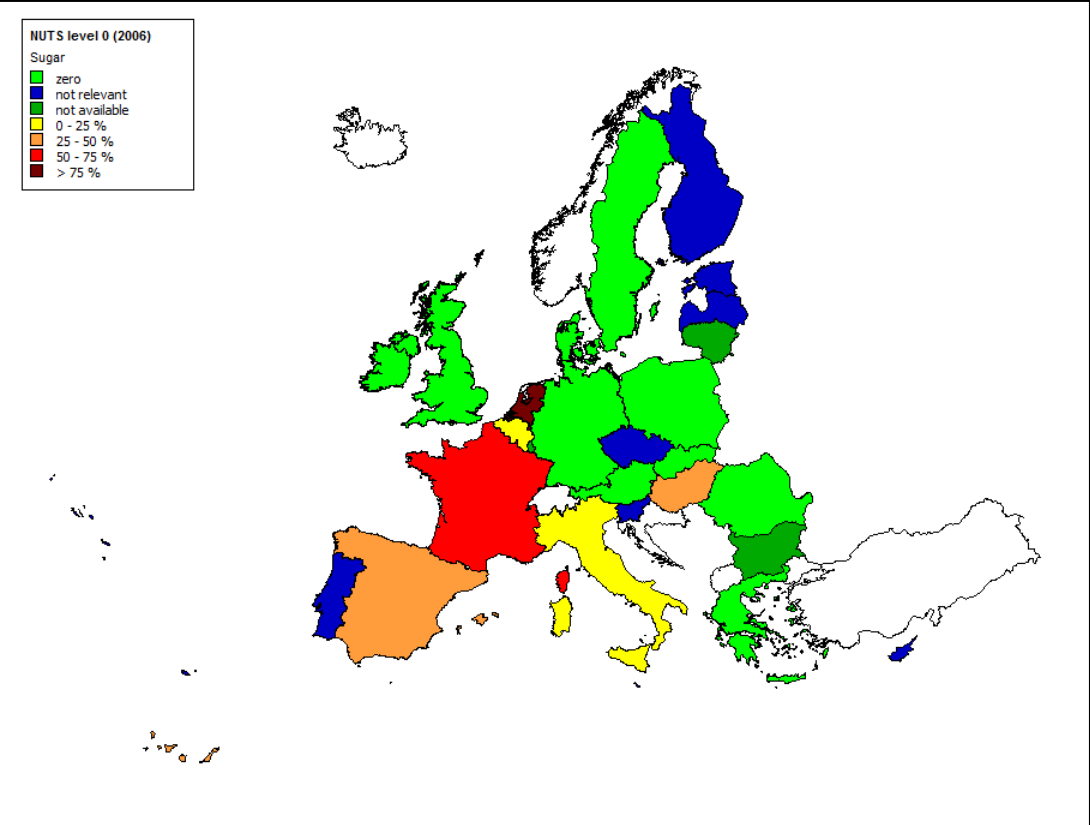


Figure 4.8. Market share of sugar cooperatives, 2010

In Eastern Europe the situation is quite different. The cooperatives are small; the number of members varies from five to a few hundred in rare case. The average turnover is only 1.5 million Euros. Four out of seven cooperatives are processing beets or marketing sugar; the other three are involved in farm production of sugar beets. Most cooperatives provide additional services to

¹⁷ We have not included these German companies in our analysis of market share by cooperatives as they are not part of the German cooperative system.

their members, such as supply of farm inputs, advisory, or provision of credit or insurance.

The EU sugar policy has had a major impact on the structure of the European sugar sector, especially on the number of countries and companies producing sugar. The effects were relatively mild in a number of countries in Northwest Europe, having large and efficient cooperatives, efficient sugar beet cultivation and mostly relatively high sugar beet prices. However also it had an impact on strategies of cooperatives and IOFs (see Chapter 6). The sugar industry is highly capital-intensive; thus avoidance of double taxation appears to be of importance.

4.9 Cereals

Cereals are an output for many (arable) farmers, but also a component of (concentrated) feed for livestock farmers. This not only complicates the data gathering on cereal cooperatives, it also means that in a lot of regions where livestock is a prominent agricultural activity, cooperatives dealing with cereals have a heterogeneous membership and transfer cereals from one group of members to the others. For the farm input and marketing cooperatives (often of the Raiffeisen type) the cereal business is one of the most important business activities, as measured by proportion of turnover. Cereal handling is very much linked to the provision of farm inputs to the same farmers, like seeds, fertilizers, and pesticides. Farm input selling cooperatives pre-finance the delivery of farm inputs and expect the farmers to deliver their cereals to the cooperative.

The performance of cooperatives as measured by market share is quite good. Strong market positions can particularly be found in the Scandinavian and West-European countries (Figure 4.9). In the last decade cooperatives have been able to increase their shares of the market.

Larger cereal marketing cooperatives and feed cooperatives entered a number of foreign countries (in particular the East European region became an investment area for German, Dutch and Scandinavian cooperatives) by acquisition of local companies, by franchising, or by merger.

In terms of strategies adopted, agricultural cooperatives are fairly defensive organisations. The cooperatives' position in the food chain is basically in the provision of market access to their members, in collecting, and bargaining for the price of agricultural raw materials. In the last decade several of the cooperatives broadened their scope by choosing to add primary and/or secondary processing. For instance in France the cooperatives in the cereal sector have not only extended their horizontal boundaries (scale economies) but also their vertical boundaries (economies of scope) by investing in added value of cereals (processing). Another example of a cooperative that has extended its downstream activities is Lantmännen, the largest Swedish cereal cooperative, which has invested in food processing of flour products and is active in the bakery sector.

In some countries the traditional organisational structure of a two-tier cooperative system has helped to improve cooperatives' position. Local cooperatives with terminals collect grain during the harvest and the secondary (central) cooperatives are collecting larger bundles for exporting or marketing to larger customers in the processing industry. Structural changes in the farming sector with the increase in average farm sizes enables secondary cooperatives that are or were mainly in the wholesale business also to enter the retail business (of farm inputs) and directly source from the farms. This process was accompanied by heavy merger activities between local cooperatives and also between local and federated cooperatives.

Some of these cereal cooperatives are very large and have thousands, or even more than 10,000 members. Concerning internal governance, it turns out that the larger the size (in turnover or number of members) of the cooperative becomes, the more the institutional governance of cooperatives deviates from the traditional cooperative model. More and more the professional management takes the final decision and there is a growing separation between the member relationship function, which is taken up by the regional councils and the operational functions, which are carried out by the management. EU regulation played an important role in the development of the European cereal sector, but it is not very clear if, and to what extent, the CAP has influenced the performance of cooperatives in comparison to IOFs.

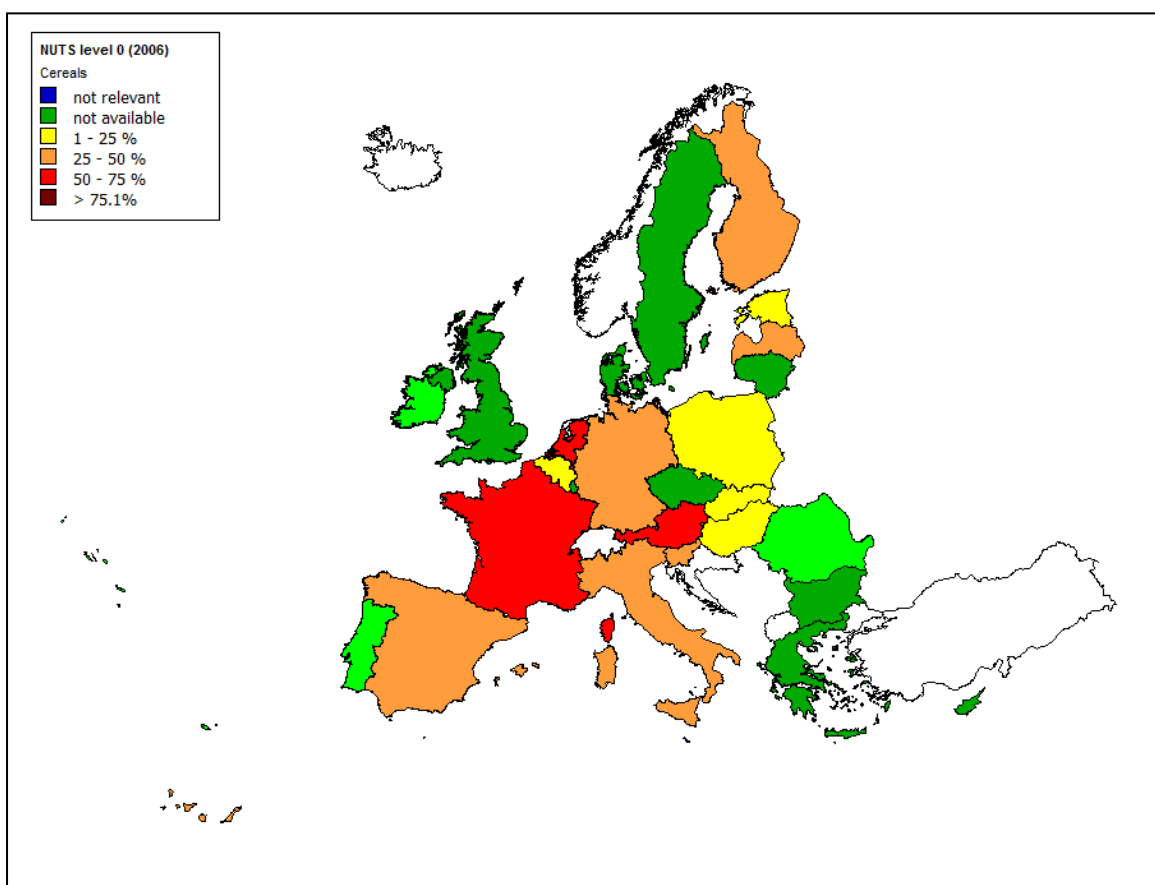


Figure 4.9. Market share of cereal cooperatives, 2010

It is not only history and culture or the policy measures that have enabled cereal cooperatives to maintain a strong position in the food chain in various countries. It is also the predominant market conditions and the flexibility in internal governance that gave cooperatives a strong position. The changing structure of agriculture also may have forced a convergence of IOFs and cooperatives' goals, governance structures, and business practices. In order to survive in the cereals sector, both types of firms had to serve the needs of a shrinking number of larger farmers.

4.10 Final remarks

In this chapter we have discussed the performance of cooperatives in eight sectors. Market shares differ strongly between sectors and Member States. Table 4.1 presents detailed figure on market shares per sector per country. This chapter has linked market shares with the characteristics of the product and the role and strategy of the cooperatives in food supply chains. We also provided some insight into the internal governance of the cooperatives and relevant policy measures. Much more information and analysis can be found in the eight sector reports (Annex 1).

Notwithstanding the large differences in market share, we see several sectors and countries where cooperatives have an important position. Figure 4.10 shows that dairy and Fruit & Vegetables are the most important sectors for cooperatives, together accounting for 60% of all agricultural produce marketed by cooperatives. Another trend is that cooperatives in many sectors seem to become more important (growth in market share) and that some take up activities further down the supply chain, with potentially more value added.

By not selecting only the largest cooperatives in this investigation, but the five largest per

country, we see a wide variety of types of cooperatives, positions in the food chain and different models of internal governance. Nearly every cooperative is different and has its own unique story. In the next chapters we provide more analysis using our building blocks (Figure 1.1.).

Table 4.1. Cooperative market shares per Member State in eight agricultural sectors (2010)

	Dairy	Pig meat	Sheep meat	Wine	Olives	F&V	Sugar	Cereals
Austria	95			15		50		70
Belgium	66	>25				83		
Bulgaria								
Cyprus				10				
Czech Republic	66	25	20	8		35		
Denmark	96	86				> 50		
Estonia	35	1				4		10
Finland	97	81				40		49
France	55	94		38		35	62	74
Germany	65	20		33		40		50
Greece		0		15		35		
Hungary	31	25	20	9		18	30	12
Ireland	99							
Italy	42			52	5	50	20	27
Latvia	33		6			12		38
Lithuania	25							
Luxemburg								
Malta	91	100		70		20		
Netherlands	90					95	100	55
Poland	72					11		7
Portugal	70			42	30	25		
Romania								
Slovakia	25	11				10		16
Slovenia	80					70		42
Spain	40	25	25	70	70	50	28	35
Sweden	100	51	55			70		
UK						35		2
EU average	57	27	4	42	37	42	27	34

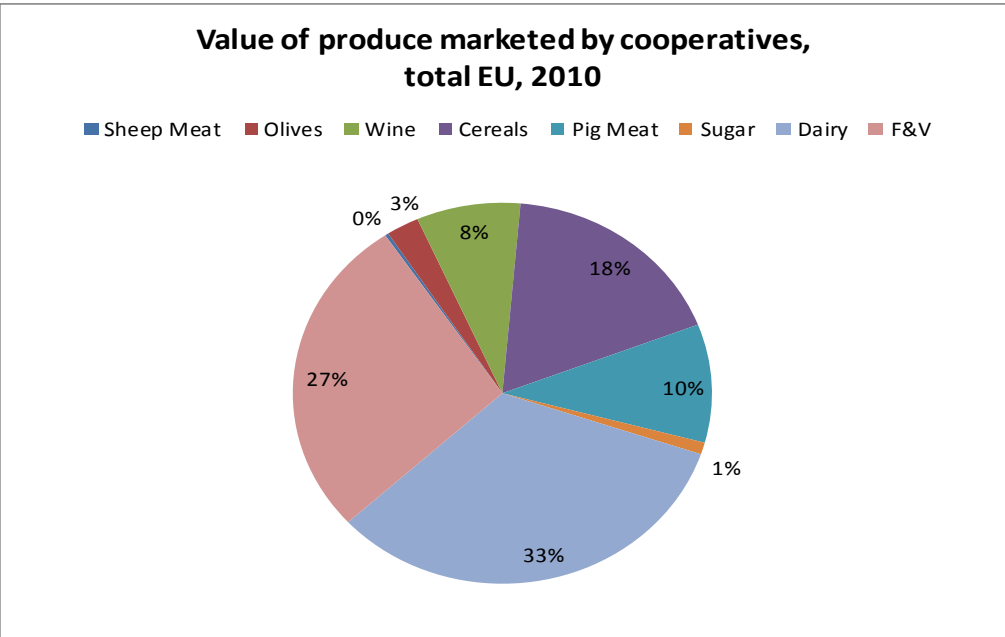


Figure 4.10. Value of produce marketed by cooperatives, for the whole EU, 2010.

5 Internal Governance

5.1 Introduction

After our overview of cooperatives in Member States and eight important sectors, in this and the next chapters we analyse the performance in terms of our analytical building blocks: internal governance, position in the food chain and the institutional environment. We start in this chapter with internal governance, and discuss how the fact that cooperatives are user-owned and controlled enables them to distribute significant benefit to their members.

The basic ownership structure of a cooperative is rather simple: the farmer-members are the owners of the cooperative firm. Owners are defined as those stakeholders that have provided the majority of the equity capital of the cooperative firm (either as upfront contribution when establishing the cooperative or as retained earnings at the end of each year) and therefore hold the residual control rights and residual income rights (Grossman and Hart, 1986). In reality, however, ownership is a much more complex and elusive issue. For example, in some countries all equity capital is collectively held, with no individual claims to parts of equity capital, in other countries member contributions to equity capital are redeemed after a number of years or at the termination of membership.

Many people would think and probably argue that “a cooperative is a cooperative, is a cooperative”. Yet, when it comes to the ownership of the cooperative firm, the various allocations of residual decision and income rights give rise to a wealth of different organisational models. Such allocations of ownership rights refer not only to farmer-patrons but also to professional, non-member managers, and non-member investors. Ownership is elusive also for another reason; it is not only about decision rights but also about income rights. Ideally these two rights go together, but in reality they may be allocated to different stakeholders.

Closely related to the issue of who owns the cooperative is the issue of who may decide on the strategies and policies adopted by the cooperative. Each member has at least one vote in a democratic decision-making structure. In practice, members have elected representatives who decide on their behalf. Thus, members have delegated decision-rights to a Board of Directors (BoD), which is the primary body to decide on the strategy and policies of the cooperative. In addition to a board of directors, most cooperatives have special committees for advising the BoD on special topics like remuneration of the leadership or accounting policies. In some countries cooperatives have a formal board of supervisors that has the formal task of control over the BoD, on behalf of the General Assembly.

While most cooperatives adhere to a basic structure of internal governance, in practice many deviations and detailed elaborations exist. For instance, in most cooperatives the actual management of the cooperative firm is left to professional managers. Different models of control over these management boards exist, e.g., the General Assembly may have delegated part of its decision rights to a member representation council. As said above, in some countries it is common (or even obligatory) for cooperatives to have a supervisory board, consisting of either only members or members and outside experts. In other countries such boards are totally absent. Another internal governance issue relates to the formal separation between the cooperative as an association and the cooperative as a firm. In several countries a legal separation is quite common, which has the advantage of reducing liability and giving the professional managers more room for entrepreneurship.

In general, the internal governance model of a cooperative is determined by the legal rules of each Member State. In several countries, the internal governance model adopted depends, by law, on the turnover of the cooperative, the diversity of its business activities, investments in international operations, and changes in the ownership structure in order to invite outside investors. However, cultural, social and historical factors also play a role in the evolution of internal governance models. More specifically, socio-cultural traditions determine the criteria by which members assess the appropriateness and effectiveness of internal governance models.

Also, insights from agency theory and transaction costs economics seem to indicate that the role of organisational culture and trust are important factors that might explain the adoption and efficiency of complex internal governance structures.

We studied the relationship between internal governance and cooperative performance in a quantitative way, but also used a more qualitatively and reflective perspective. The latter includes comparisons among countries and sectors, as well as comparisons among clusters of cooperatives. Particular attention has been given to the legal analysis of internal governance frameworks and their application in practice, asking the pivotal question: “Does law matter?”. Figure 5.1 shows the assumed interaction between legal frameworks, international governance systems and the evolution and performance of farmers’ cooperatives.

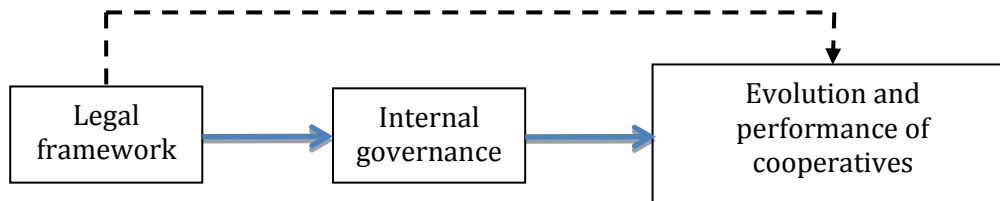


Figure 5.1. Interaction between laws, internal governance and cooperative performance

The theoretical and empirical problems related to the internal governance of cooperatives cannot be fully addressed by applying one “grand theory”. Not all of the problems identified by the governance literature on publicly-owned firms apply equally to cooperatives and other democratic membership organisations. Furthermore, because cooperatives lack most of the external mechanisms that help monitoring listed corporations, cooperatives may even have to develop more complex and diverse mechanisms of internal control than their corporate counterparts. In some contexts, the application of the agency theory approach might even be counterproductive because the board of directors may fulfil functions that clearly diverge from the agency approach’s postulates. For instance, the board may function as a political institution reducing the cost of conflicting interests among different groups of members. In other situations, the board may serve as a group of expert advisors or a resource network available to the management. As cooperatives are user-owned companies, the board is, in the first place, representing the users.

Cornforth (2004) suggests applying “a paradox perspective” in order to highlight the main problems of internal governance and the main tensions that arise:

- The tension between member representation in interest groups and the need to recruit “expert knowledge” from outside.
- The tension between performance goals and conformance with accountability and prudence.
- The tension between the needs of controlling and supporting the management.

In this chapter we will first provide some data from our sample of 500 cooperatives (see Chapter 2) on internal governance, shed light on the aforementioned issues. We then discuss the diverse ownership structures that are (increasingly) adopted by agricultural cooperatives in the EU. We will use the term hybrid ownership structure as many cooperatives combine ownership characteristics of the traditional cooperative with those of other legal forms, most notably the corporation.

For the same reason in section 5.3 the internal governance of agricultural cooperatives in the EU is discussed in more detail, based on our legal analysis and the case research. While ownership structures can be classified in a limited number of specific categories, often defined by legal restrictions, the diversity in internal governance structure is much broader. Both in terms of member involvement in decision-making and in terms of delegation of decision rights to professional managers, agricultural cooperatives are characterised by a significant

heterogeneity, which cannot easily be classified in generic typologies. The last section of the chapter discusses the relationship between internal governance and performance, on the basis of our empirical assessment.

5.2 Data on internal governance

The performed statistical analysis reveals the key characteristics of the contemporary cooperative system and its internal governance features in the EU-27. Overall, cooperatives in the EU are still serving a mainly regional membership, while their activities are rather specialised. Most of them trade predominately with their members, about 90% of whom are active. Roughly a fifth of the cooperatives in the sample use a holding structure. In only 14% of the cooperatives, professional managers serve on the board of directors. Decisions on who is eligible to serve on the board of directors are mostly based on expertise. In more than 60% of all cooperatives the operational business is run by professionals. Cooperative supervisory boards contain outsiders (non-members) in about a quarter of the cases. About 80% of all cooperatives in the sample still used the one member one vote principle. Only 20% of the sample use proportional voting, of which half apply an upper limit to the number of votes one member may hold. Around 12% of the cooperatives have subsidiaries, and more than half of the cooperatives do engage in trade with non-members.

5.3 Hybrid ownership structures

Hybrid ownership structures are called hybrid because they do not strictly follow the user-owned, user-controlled and user-benefit principles. We distinguish two different kinds of hybrid ownership structures. First, cooperatives increasingly invite non-users to participate in the cooperative as a whole or in one or more of their subsidiaries. Thus, outside individuals and organisations become co-owners of (a part of) the cooperative's assets. These outside owners can also be farmer organisations (or farmer unions) which represent a larger group of farmer than just the users of the cooperative. Second, there are hybrid ownership structures where a firm is owned by farmers or by one or more farmer organisations but it does not have the legal form of a cooperative.

Type 1: Outside owners

While in the traditional cooperative equity capital is supplied only by members, in hybrid structures also non-members provide equity capital and thus claim a share in the profits of the cooperative. Non-traditional cooperative structures adopt various financial structures, in which income rights and sometimes also decision rights are allocated to outside investors. Well known typologies of different ownership structures (focussing on the providers of equity capital) have been developed by Nilsson (1999) and Chaddad and Cook (2004).

Nilsson (1999) distinguishes among five models of financial structure of the cooperative (Table 5.1). The main distinction among these five models pertains to ownership rights, where owners are the actors that provide equity (or risk) capital to the cooperative and thereby become the residual claimants of the surplus of the cooperative. Ownership rights can be collective or individual and can be held only by members or by members and external investors.

Model 1 is called the "traditional cooperative"; only members invest in the cooperative and all equity capital is collective. This means there are no individual ownership titles. Model 2, the "participation share cooperative", has partly individualised its equity capital; members may also become individual shareholders in the cooperative and these shares may be traded at an internal share market. Model 3 is the "cooperative with subsidiaries" in which outside investors participate. Equity capital is partly collective, partly individual, and both members and outsiders own shares in the subsidiary. Model 4 is the "cooperative with proportional tradable shares". In the United States this is called the new generation cooperative. Only members are shareholders, and all equity capital is individually owned. Finally, Model 5, the "PLC cooperative", is listed at a

stock exchange, and outsiders may own and trade the common stock.

Within our framework, only models 3 and 5 are hybrid ownership structure because only these models have ownership by non-members.

Table 5.1. Financial structures of cooperatives

	Type of Equity Capital		Providers of Equity Capital	
	Collective	Individual	Members	Non-members
1. Traditional cooperative	X		X	
2. Participation share cooperative	X	X	X	
3. Cooperative with subsidiaries	X	X	X	X
4. Proportional tradable share cooperative		X	X	
5. PLC cooperative		X	X	X

Source: Nilsson, 1999

Financial structures can become very complex. An example of the model 2 (Participation share cooperative) is the (historical) case of the Dutch second-tier cooperative Cebeco. Cebeco had invited an investment bank to become a so-called capital member of the cooperative. The Netherlands Investment Bank (NIB) supplied 60 million euro of equity capital and in return it received a fixed annual interest on its investments. The shares were preferred shares. Although NIB became a member of the cooperative, its voting rights were more restricted than those of the regular members (they could only be used when financial performance was below a certain threshold). Other examples of hybrid ownership structures can be found among German and Austrian sugar cooperatives, but also in the Finnish meat sector.

Due to complex ownership structures it is not always clear whether producers (still) have the majority of ownership and control, especially if the composition of the producer organisations that own the “cooperative” is not clear. Examples are the German sugar companies Südzucker and Nordzucker. Südzucker is the largest sugar producer in Germany and in the EU. Südzucker has the legal form of an Aktiengesellschaft (AG). It is a shareholder company publicly listed at the stock exchange. Südzucker has a complicated shareholder structure. The Süddeutsche Zuckerrübenverwertungs-Genossenschaft eG (SZVG; South German sugar beet processing cooperative) holds 56% of the shares. The members of SZVG are a number of regional sugar beet growers’ associations and a number of federated cooperatives like BayWa and DZ Bank. The sugar beet growers hold 51% of the shares. Other investors include Austrian shareholders, via Zucker Invest GmbH, with 10%. The remaining shares of 34% are widely held.

A cooperative that can be characterised as hybrid in several ways is the Finnish transnational meat cooperative HKScan. HKScan is a publicly listed company, having a number of minority owners that have no linkage to farming and/or the meat industry. One of the main shareholders is the cooperative LSO Osuuskunta, a cooperative of animal farmers. Almost half of the members of LSO Osuuskunta are cattle farmers, almost half are pig farmers and a small group are poultry farmers. Another important shareholder is the cooperative of the Swedish pig farmer-suppliers. As this cooperative does not have assets itself, it can also be considered a producer association. Also the Finnish Farmers’ Union MTK has a participation in HKScan. Even the Danish competitor meat company, Danish Crown, is a (small) shareholder of HKScan.

HKScan has two types of shares: those representing income rights and those representing decision rights. While the Finnish producer cooperative LSO Osuuskunta has about 35% of the income rights (A shares), it has 70% of the voting rights (KII shares). Thus, one of the important elements of this hybrid model is that although farmers do not have the majority of income rights, they still have the majority of decision rights. This has been called the Finnish model of hybrid ownership structure, as compared to the Irish model of ownership structure where income rights and control rights in the Plc cooperative are symmetric (Van Bakkum and Bijman, 2007).

A number of developments in the Finnish pig meat industry, in the 1980s and 1990s led to

the hybrid ownership structure of HKScan. The first step in the hybridisation process was in 1988, when the LSO cooperative established a limited liability company, named LSO Food Oy, to which all slaughtering, processing and marketing activities were moved. In the early 1990s LSO Food Oy took over several slaughtering companies (acquiring well-established brands), and as a result needed additional equity capital. This capital was obtained from outside investors, by becoming listed, in 1997, at the Helsinki stock exchange. The name of the company changed to HKScan as a result of the acquisition of the Swedish slaughtering company Scan AB, in 2007.

Type 2: Non-cooperative, farmer-owned companies

In several EU countries, farmer unions and other farmer organisations are (co-)owners of companies that process farm products or provide inputs to farmers. Three examples are VION in the Netherlands, AVEVE in Belgium, and OVEKO in the Czech Republic.

VION is a Dutch meat company, fully owned by the Dutch farmers association ZLTO (through its investment company NCB). VION was established in 2002 and, within ten years, it has become the largest meat company in Europe. When ZLTO decided to build a meat company, the main slaughtering company in the Netherlands was Dumeco, partly owned by cooperatives, partly by private investors, partly already by ZLTO. Most of the other owners did not want to make additional investments, which were deemed necessary in order to become a major player in the European meat industry and become a strong supplier to the concentrated retail. ZLTO was in a position to make large investments in the meat industry because it had substantial reserves earned partly by selling insurance company Interpolis to Rabobank (in 1990) and partly because its subsidiary Rendac in rendering had earned large profits. Although VION is sometimes seen as a cooperative, it does not fit our definition of the cooperative, as it is not user-owned and user-controlled. The farmers that supply pigs to VION represent a minority in the farmers' organisation ZLTO, and therefore have no control rights over VION.

AVEVE is a Belgian feed company, fully owned by the Flemish Farmers' Association (Boerenbond). Formal ownership is through MRBB, the financial holding company of the Boerenbond. Ownership by the Boerenbond, compared to shareholders outside the farming industry, guarantees the continuity of the organisation because the owner has a long-term commitment to the industry. Farmers have some influence on the policies of AVEVE through district boards (regional advisory boards). As a farmer-owned company with a strong position in the feed industry, AVEVE acts as a competitive yardstick in this industry; IOFs have to follow closely the prices and services provided by AVEVE in order to survive.

The Flemish Boerenbond, through its investment fund AIF, also has a 10% participation in Pinguin Lutosa, a Belgian IOF specialising in the development, production and marketing of deep frozen products (vegetables, potatoes, ready-to-eat meals, etc.). Having insight in that supply chain is one of the reasons cited for this participation. Pinguin Lutosa had a turnover of 500 million €. AIF also has invested in Covalis, the largest Belgian company in slaughtering and processing pigs and cattle. COVALIS is a subsidiary of COVAVEE cvba, a cooperative of 600 pig farmers, with 25% share of the Belgium pig meat market.

Actually, in many EU Member States examples can be found of farmer organisations owning companies that process and market the products of (part of) the members of that organisation. For instance, in the Czech Republic, the Association of Sheep and Goat Producers is the majority shareholder of the marketing firm OVEKO, which holds 20% of the commercial sheep meat market. As our research did not focus on such farmer-owned business, we can only provide some anecdotal evidence.

In conclusion

From these examples and some more discussed in the case study reports and in the literature, we conclude that modern cooperatives (particularly the larger ones) represent a much more complex organisation than the archetypal traditional cooperative. These empirical observations suggest the difficulty of capturing in a single definition the various, complex economic, social, and legal aspects of this unique institutional arrangement. Imposing definitions on cooperatives might result in stealing them of the flexibility necessary to adapt to dramatic changes in their

economic and social environment. The observations also imply that farmers have a lot of options on how to organise their interests in cooperative forms, assuming that the national law affords them this freedom. This is the topic of the next section.

5.4 Internal governance: trends and legal issues

Transnational and international cooperatives

The legislation on internal governance does not seem to pose any substantive barrier to cooperatives interested in expanding their operations internationally. However, the internationalisation of cooperatives raises the question of the cooperative character and identity, as many international cooperatives do not adhere to the principle of open membership. They often exclude foreign suppliers from entering the cooperative, for a number of reasons (see Chapter 6). Cooperatives going international adopt diverse ownership structures while internationalisation renders new financing techniques and governance structures necessary. Foreign units are treated primarily as profit centres that support growth and benefit current members.

Mergers between cooperatives do not necessarily lead to the hybridisation of the cooperative structure. However, cooperatives that actively entered into the market for mergers with cooperatives or acquisition of IOFs, or made investments in IOFs, realised the need to attract significant amounts of risk capital. From an internal governance point of view, an interesting result is that in some of these cases the strategy had not been sufficiently discussed with the members of the cooperative, and has led to failed mergers.

Cooperatives that internationalise leave the internal governance structure of the cooperative itself untouched. Cooperative members are reluctant to allow agricultural producers that deliver to the foreign subsidiary becoming members, because they are not willing to accept changes in the ownership structure of the cooperative.

Outside investors

Another aspect with regard to the question whether international cooperatives are still considered real cooperatives relates to their financing, especially in those cases that equity capital has been raised from outside investors at the level of the sub-holding subsidiary through the issuance of tradable shares (e.g., in the cases of Südzucker and BayWa). As long as there is an upper limit on the number of shares available for trading and the free float does not exceed 49%, from a legal point of view the cooperative is still controlled by its users, although it has to take into account the interests of the other owners. In these cases, however, there is a risk that members gradually lose effective control, especially over major transactions at the level of the sub-holding. A comparative analysis on legal aspects indicates ill-defined control rights of members in this respect. It is also striking that a document analysis of annual reports of BayWa reveals that the word “member” is not used. However, the cooperative legislation of the individual Member States seems to provide sufficient facilities to incorporate clearly defined control rights in the bylaws of the cooperative. Members should be aware of this associational freedom to reorganise the internal governance through the adjustments of the cooperatives’ bylaws.

This is not a theoretical issue, because research strongly indicates that traditional cooperatives show lower performance while cooperatives with outside owners show higher returns. So it can pay for farmers to take up new ventures with their cooperative (see also next chapter). In the case of Greece, for example, we identified a direct negative link between a constantly amended, albeit in inefficient ways, law and cooperative performance. In France, the legally enforced restriction of cooperatives’ operations within geographic regions seems to have reinforced members’ commitment to their cooperatives.

New Member States

In regions with emerging new cooperatives as well as in the New Member States, emerging internal governance issues are quite different from those faced by older or well-established

cooperatives. We find support for the argument that policy measures and internal governance should reflect or be able to take into account the different stages of development of cooperatives.

A critical issue that puzzles cooperative development experts is whether existing successful organisational models are transferable to other legal, economic, social and cultural contexts. The information and data collected for this study suggest that this can happen if, and only if, the local needs and particularities are well understood and taken into account. Although the lack of trust and leadership was the common denominator in all case studies on emerging new cooperatives and cooperatives in the New Member States, the cooperatives have followed diverse evolutionary paths in each of the cases studied.

Education is essential to cooperative development as well as adequate advisory services and financial support. According to local cooperative experts, there exists a strong demand for professional management as well as well-trained members of the supervisor bodies. In some of the Member States such needs have not been sufficiently accommodated by the national cooperative laws.

In some of the Eastern European Countries, the cooperative actually functions as a hybrid that encompasses elements of both farmers' association and labour cooperative. From a policy point of view, this is an important finding, since the incentives within a labour cooperative are different from those of an agricultural producer cooperative. The communist legacy persists as the lack of trust and leadership are common obstacles to cooperative development. From a legal perspective, this implies that national codes have to take into account the peculiarities of a Member State and therefore, a "one size fits all" approach might not work. Further research has to be conducted on the development of model codes/statutes that are flexible enough and are able to take into account the different stages of a cooperative's development. Access to credit, human capital and the market are main issues in developing areas.

Conflict of interests

Internal governance should also address the issue of conflict of interests. Especially, in small cooperatives the risks of self-dealing (elite-capturing) and moral hazard has to be solved to protect (minority) members. There is some evidence that larger members with more knowledge, experience and financial capacity are the ones to be active in the board of cooperatives. Rules to solve conflicts of interests in general are ex-post remedies and sometimes ill or not at all defined. Cases of self-dealing may also arise from the weak monitoring function of the board of directors, composed by members that have delegated the day-to-day management of the business to a managing director, who has no formal authority as a board member, but as an employee. So the traditional model is far without risk, supporting the case that trust and reputation combined with professionalism on the board is pivotal for effective internal governance. Too much trust could easily result in a lack of effective monitoring of the board. Trust is gained and social capital built up when it is clear to members that internal governance is effective.

We also find that proper remuneration of managers is important in this respect. Managerial compensation is very diverse according to the size of the cooperative. Small cooperatives seem to have trouble attracting professional management. Training of professional management is an important aspect. However, this situation is not comparable with the situation of large transnational and international cooperatives, where members of the management are selected from the market for managerial expertise, where large dairy cooperatives compete with IOFs like Nestlé, Danone and Unilever for professional managers in the food sector. In those cases it is important that the management understands the cooperative character of the enterprise and acts accordingly.

Legal issues that relate to internal governance

From a legal point of view, several issues are identified as important. For example, how accountable the board remains to members while making key strategic decisions? Related questions that have been raised include the following: Are farmer-members of large cooperatives that adopt a holding-like structure or own several subsidiaries, still in charge of key strategic decisions? How are formal decision rights that would ideally be allocated to the

member-patrons as residual claimants allocated in practice? Do members still perceive the adopted internal governance structure as providing them with the means to exercise effective control? Cooperatives should address such questions if they seek to strengthen member commitment.

Internationalisation, but also diversification, correlates with changes in internal governance and ownership structure. Two developments with regard to large international and transnational cooperatives surfaced. First, the internal governance of these cooperatives evolved towards a multi-layered governance structure with a clear distinction between the associational part in the cooperative and the entrepreneurial part in the sub-holding. Second, the centre of decision control has been transferred to the management. The consequence of these developments is that decision control rights of members have become weaker and that members have lost (part of) effective control.

In general, the legal frameworks for internal governance in the Member States do not hamper the development of cooperatives. Yet, the increasing complexity of internal governance models in practice is not reflected in the law, leading to a discrepancy between formal control and effective control by members. Looking at the cases of international and transnational cooperatives, mainly a Northwest European phenomenon, shows that cooperative legislation in these countries provide sufficient legal flexibility to address internal governance needs through adjustments of the bylaws. Actually the legal frameworks in countries like The Netherlands and Denmark are extremely flexible. This has given cooperatives sufficient flexibility to adapt their bylaws. However, with regard to strategic decision-making one may wonder whether the legal framework provides sufficient safeguards for member involvement, in particular when major decisions on strategy and structure are taken at the level of the sub-holding subsidiary.

National cooperative law provides for a business organisational framework that is able to take into account the different stages of cooperatives' evolution. This, however, may not be true for all the New Member States, where access to best practices is more difficult and laws or model codes for bylaws could transfer knowledge and support learning. Several internal governance issues were identified that hamper the sound development of cooperatives in these countries: the absence of professionalism on the board of directors and supervisory board, the lack of a clear mandate to introduce a supervisory body monitoring the board, the lack of knowledge of and experience of members with cooperative governance, as well as a lack of knowledge of financial monitoring.

In some southern Member States (Portugal, Spain and Greece), specific issues with regard to internal governance possibly influence the performance of cooperatives negatively, in particular because internal monitoring and control is underdeveloped due the lack of clear legal mandates on supervisory boards. In some cases this makes the chairperson of the cooperative vulnerable to legal consequences. Especially, in small start-up cooperatives the traditional internal governance model of a general assembly and a board of directors needs to be complemented by transparent rules that address conflicts of interests.

5.5 Internal governance and performance

We also studied the relation between internal governance and cooperative performance by performing a regression analysis. This resulted in several interesting insights. Our models suggest a strong rather negative effect of size (measured in number of members) on turnover per member. In other words, cooperatives with a small membership perform better than cooperatives with a large membership. Cooperatives operating as a holding – in contrast to a single legal structure – and cooperatives where operational business are managed by professional managers, perform better. In contrast to the findings of the corporate governance literature on IOFs, in our sample of cooperatives a positive effect of board size is identified. A larger board improves performance – despite the theoretically higher costs of coordination and decision-making. In line with the general literature, outsiders serving on the supervisory board have a positive effect on performance. In addition, we find a negative effect of regional representation as one out of three criteria for serving on the board of directors, while expertise

and product representation have a positive effect.

These findings show that professional structures and policies regarding board composition and member incentives affect performance. At the same time by comparing with the literature we can show how cooperatives differ from other types of firms in important aspects. In our sample the typical attributes of “professionalising cooperatives” like for example proportional voting rights, professional management, supervision by outsiders, and selection of directors based on expertise or product representation as opposed to regional origin, all have a positive effect on cooperative performance. We conclude that our results support the relevance of our general study concept in which the institutional environment together with the position in the value chain and internal governance determine crucial factors of success and therewith potential entry points for supportive policies.

Sector characteristics

Looking at the differences in proportions between sectors also gives some interesting insights. Sectors differ widely in how they professionalise their board structures. For example, more than 20 per cent of the meat cooperatives have professionals serving on the board, while less than 3 per cent of the wine cooperatives employ professional managers.

In many aspects the dairy sector significantly differs from the other sectors. For example, most of the cooperatives organised in a holding structure can be found in the dairy sector. Structure-strategy considerations known from the theoretical literature may provide an explanation (Nilsson, 1999). An ever concentrating market, a history of intense mergers, competitive pressure and the need to realise scale economies may all partly explain this phenomenon.

Dairy also differs from other sectors with regard to the structure of dairy cooperatives. A quarter of the dairy cooperatives has subsidiaries. The importance of internationalisation in this sector can explain this difference (Harte and O’Connell, 2007). Dairies in the sample also have relatively more members and higher turnover and they less frequently trade with non-members, while for example cereal cooperatives trade much more with non-members and less frequently demand exclusive member patronage. Different marketing pools and differentiated cost policies exist less frequently in dairies while, for example, the fruit and vegetables cooperatives pay less frequently volume premiums.

6 Position in the food chain

6.1 Introduction

The position of cooperatives in the food supply chain refers to the competitiveness of cooperatives vis-à-vis other chain actors, such as processors, wholesalers and retailers. It includes sector- and product-specific aspects that have a significant influence on the contracts that parties enter into, on relevant policies, but also the structure of agriculture itself. An important choice that affects the position of cooperatives in the food supply chain is the type of strategy that cooperatives pursue.

In section 6.2 we summarise our findings based on the analysis of data on 500 cooperatives and present a number of selected issues. In section 6.3 we focus on the issue of structure and strategy in cooperatives in several Mediterranean countries. In the previous chapter we already reported on some internal governance issues with respect to Mediterranean countries and our data suggest that for instance in wine there is a dual structure in strategies (see next section). At the same time, some very successful agricultural cooperatives are based in Mediterranean countries, which have adopted different strategies. Section 6.3 elaborates on this issue and generalises our findings. Next, and not unrelated, is the issue of second tier (or federated) cooperatives: agricultural cooperatives that are owned by primary agricultural cooperatives whose members are farmers.

Section 6.5 is devoted to bargaining associations. This type of organisation can be found particularly in the F&V and dairy sectors. The major objective of these organisations is to improve the bargaining power of farmers' vis-à-vis suppliers, processors and retailers. They explicitly pursue the goal of building countervailing in the food chain. In section 6.6 the performance of dairy cooperatives is analysed in more detail, to answer the question whether a high market share of cooperatives influences the prices received by members and by non-member farmers. We conclude the chapter with the issue of financing the cooperative.

6.2 Data on the cooperatives' position in the food chain

There are quite a large number of differences in the cooperatives' position within single countries and between sectors. As product characteristics and sometimes the CAP crucially affect the role that cooperatives play in the food chain, we first summarise key facts per sector identified in this study (see also Chapter 3).

Cooperatives in the *cereals supply chain* primarily provide their members with access to markets by collecting raw produce and by bargaining terms of trade on behalf of their members. In the first decade of this century nearly all functions performed by cooperatives became more relevant. Several cooperatives broadened their scope by choosing to add primary (and/or secondary) processing. Within this sector cooperatives' performance measured by market share is quite strong (see Chapter 4).

Marketing cooperatives in the *dairy sector* are strong competitors on the markets, by being active in almost all parts of the food supply chain. They provide markets to their members as well as produce branded or private label products and sell these directly to retailers. Dairy cooperatives in Europe perform quite well. In thirteen EU-countries they command more than 50% of the market (measured in milk volume collected in first-handling and processing stages). Cooperatives have increased their market shares relative to IOFs in those countries where they already had a high market share.

Producer organisations in the *fruit and vegetable* sector cover the whole range of different functions with the most important being the provision of market access, the collection and marketing of products, and secondary processing. Cooperatives in four countries have a comparable high market share (95% in the Netherlands, 83% in Belgium, 70% in Denmark, and 68% in Slovenia). In all other European countries cooperatives face strong competition from powerful IOFs. The F&V industry of EU countries face increasingly intensive international

competition as logistic technologies allow products to be shipped over longer distances and to be preserved for longer periods. Cooperatives have a strong position in the *Olive oil* sector. Wholesaling used to be, and still is in several cases, their major pursuit, but value-added activities have increasingly become their major focus. Cooperatives' position varies dramatically by olive oil producing country. In Italy, cooperatives have not been very successful in adding value to the product and, consequently, their market share dropped from 13% in 2000 to 5% in 2010. Spanish cooperatives still have the highest market share (70%) but, like their Italian and Portuguese counterparts, they are losing market share to IOFs.

Two types of cooperatives coexist in the *wine sector*. The first refers to a group of dynamic, market-oriented cooperatives, which have successfully addressed various market-related challenges by investing heavily in branding and offensive marketing strategies. In contrast, the second group of cooperatives remains focused on producing bulk wines and bargaining terms of trade on behalf of their members. In terms of market shares commanded, wine cooperatives perform better than IOFs in Slovenia (71%), Spain and Malta (70%), and Italy (52%).

In the *wine sector* two types of cooperatives exist. There is a so-called dual structure, with coexistence between a group of dynamic market oriented cooperatives that have managed to deal with market changes and strong branding and marketing activities in contrast to many cooperatives that are dedicated to production and collecting/bargaining products. Compared to IOFs, wine cooperatives perform (measured in market shares) well in Slovenia (71%), Spain and Malta (70%), and Italy (52%).

The position of cooperatives in the *sugar sector* seems to be strong and they cover nearly every function in the food supply chain. For regulatory reasons, sugar cooperatives provide markets for their members and they are also strong in the processing and marketing.

Cooperatives in the *pig meat* sector are serving nearly every stage of the food chain, from transport and storage to primary and secondary processing, marketing of brands, and wholesaling. Cooperatives in five European countries have more or less outperformed IOFs (Malta, 100%; France, 94%; Denmark, 86%; Finland, 81%, and Sweden, 51%).

Not all EU countries have a significant *sheep meat* sector. In those countries where sheep meat is an important commodity, cooperatives' functions are closer to primary production than to final consumption. They include guaranteeing market access, collecting members' products, and wholesaling. Marketing of branded products is as rare as secondary processing. Yet, our case study research has identified some very successful sheep cooperatives that do perform such functions (Oviso in Extremadura, Spain and the ANM Group in Scotland, UK). The large number of small producers and low demand make the organisation of large scale production a very complex issue.

Four different options for growth strategies were identified: autonomous growth, horizontal mergers, vertical mergers & acquisitions, and international mergers & acquisitions (M&A). A bit of a surprise is that in all sectors growth strategies rely to a high degree on autonomous growth (increasing turnover by extending the current market and selling more or attracting new members). Given the concentration process in the cooperative sector in many EU countries, it was expected that the common way of growth were mergers (with neighbouring cooperatives) and not autonomous growth. Probably this is due to the respondents' reluctance to reveal their intention to merge with or acquire a neighbouring cooperative. A further explanation may be that many mergers of cooperatives are not the result of a deliberately chosen strategy but of poor performance or take-overs in times of financial hardship.

For the cereals and dairy sector horizontal M&A is the second most important strategy. Not surprisingly, vertical and international mergers and acquisitions explain cooperatives' growth only to a minor extent. In the cereals, sugar and, to a minor extent, in the pig meat sectors cooperatives consider low cost to be the key competitive advantage for success, as opposed to the dairy and wine sectors who highlight value creation by product or service differentiation. Cooperatives in the olive oil and fruit and vegetable sectors use both strategy types, while cooperatives in the sheep meat sector tend to focus on a niche market by serving a narrow set of customers (Figure 6.1).

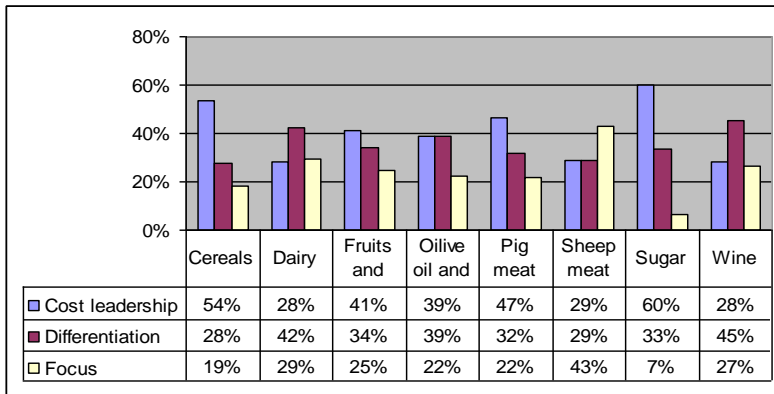


Figure 6.1 Percentage of cooperatives per sector that have a cost leadership or differentiation or focus strategy, 2011

The analysis of the branding activities performed by cooperatives also shows sector specific differences (Figure 6.2). In the wine sector cooperatives' turnover is basically the result of sales of branded products. In this sector, the establishment of own brands has a long tradition and it is a strategy adopted by most cooperatives (although some are bargaining associations that sell grapes). Dairy cooperatives invest and promote also their own brands, but there is still a larger number of dairy cooperatives with a smaller proportion of branding activities. In both sectors cooperatives are part of the final market where the supply of own brand products and the ability to produce private label products is a requirement. Sector specific characteristics explain the low degree of branding activities in the cereals, sugar, sheep and pig meat sectors. With some notable exceptions these products are hardly sold as a branded product in the retail market.

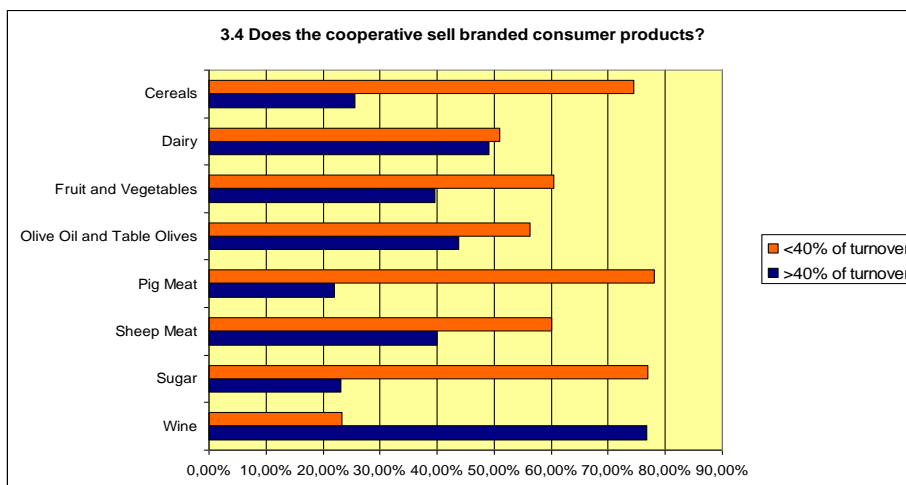


Figure 6.2 Percentage of cooperatives per sector that has a low (<40%) or high (>40%) percentage of its turnover in branded products, 2011.

6.3 Strategy and structure in the Mediterranean

In a competitive market environment, a cooperative like any other company needs to choose its corporate strategy (for the organisation as a whole) and its business strategies (for divisions and subsidiaries). As we are dealing with cooperatives in the food chain, an important element of strategy is the marketing strategy.

Choosing a particular strategy often implies choosing a proper structure. Although the basic structure of farmer ownership and farmer control cannot be altered, other elements of structure may need to be adjusted when pursuing a particular strategy. For instance, following a cost leadership strategy usually requires having access to capital that is needed to make the

necessary investments in large scale, low cost production and processing. Also having efficient distribution channels is essential in a cost leadership strategy.

The issue of the interaction between strategy and structure of the cooperative was explicitly studied in a number of Mediterranean cases; fruit and vegetables in Spain, olive oil in Greece and Spain, wine in Greece and France. In addition, the interaction between territorial embeddedness and a niche marketing strategy was studied for French cooperatives.

Degree of vertical integration

Our analysis shows that vertical integration is a necessary but not sufficient condition for better cooperative performance. Even though the degree of vertical integration is positively associated with higher producer income, several intervening structural and strategic variables, including the structure and performance of the industry/sector at hand, affect the success of this strategy. Possession of strategic capabilities and resources in the form of natural resources, spatial considerations, path dependencies, entrepreneurial orientation and the quality of cooperative leadership are all important determinants of the performance of a cooperative and interact with a vertical integration strategy.

Control of supply seems to be necessary in order to benefit from vertical integration. Otherwise the cooperative is side-tracked by the duty to sell excess produce (that also can be produced additionally by farmers if the cooperative is successful in increasing prices) and, consequently, constrains its vertical integration strategy or makes the adoption of a complementary strategy of low cost, necessary.

This also implies that differentiation may become more attractive when a cooperative has access to only a limited total supply of a product (e.g., in the case of PDO or other specialty products). Moreover, changes in the external environment might force a cooperative to adopt a mixed strategy that combines cost leadership in one market segment and product differentiation in another. The example of EFC (see section 6.5) has shown that full control over the supply of a specialty can generate higher producer prices. The French system of linking cooperatives to a territorial boundary reinforces governance and strategy, but does not solve problems of finance or the need to convince young farmers to take a leadership role in the cooperative. A similar system in Spanish wine did not work.

The need for innovative ownership, governance, and capital acquisition methods

The need for the introduction of new ownership structures as well as capital acquisition and management methods is imperative. Our analysis shows that the traditional risk-avoiding, less entrepreneurial cooperative model is associated with poor economic performance.

In order to adopt differentiation and niche market strategies, reach high-end markets and thus receive a higher percentage of the value generated, cooperatives in regions that can produce an exceptional product (e.g., based on traditional old olive groves) must adopt capital intensive marketing and promotion strategies. In light of this, the ownership structures they adopt should provide members and other stakeholders with strong incentives to adequately finance the cooperative.

The traditional cooperative model is associated with a vaguely-defined property rights structure, which results in little incentive for members to invest in their cooperative (Cook and Iliopoulos, 2000). Yet, growth, particularly in the value-added segments of food supply chains, can only be achieved through major capital investments in both tangible and intangible assets. Therefore, cooperatives interested in maximising the rents accruing to their members should consider one of the numerous innovative ownership models adopted by agricultural cooperatives in North America, Oceania, and North-western European countries during the last 25 years (see also Chapter 5 on hybrid ownership structures).

In addition to the risk capital needed to finance growth, cooperatives also need to have access to working capital. In some countries and regions, the presence of credit cooperatives has proven to be an effective institution for financing marketing cooperatives, one which allows optimum knowledge of both the sector and the members, and allows careful financial monitoring. In regions and sectors where such institutions are not available, cooperatives face

significant financial constraints. Moreover, in these cases cooperatives have failed to scale up and take advantage of sound business opportunities.

The above point leads to a relevant issue for agricultural cooperatives, that is, how they obtain risk capital in order to finance export and growth strategies. Innovative ownership and governance structures as well as financing techniques, already adopted by other European cooperatives, could also be adopted by cooperatives in other sectors and regions. Example of structures and changes that may be adopted in order to overcome perceived capital constraints include, but are not limited to, collaboration with IOFs or other cooperatives, or the setting up of marketing subsidiaries, joint ventures, new generation cooperatives, etc. Some European cooperative laws allow for different classes of investors and more information (extension) on the success or failure of such investments, and member relations departments established by cooperatives would be useful for all agricultural cooperatives in the Mediterranean area.

Collaboration between cooperatives and IOFs

Collaboration with IOFs may lead to better cooperative performance if coupled with a relatively strong competitive position of cooperative within the chain. Otherwise, opportunistic behaviour of the IOF is probable.

In all of the cases where cooperatives have benefitted from collaboration with IOFs when entering the agreement, the cooperative had already secured a relatively or absolutely strong position in the supply chain. On the other hand, in the cases where cooperatives had a relatively low bargaining power vis-à-vis IOFs in the industry, the collaborative arrangement seldom lasted for more than a few years due to the opportunistic behaviour of the partner with the stronger bargaining power.

Federated cooperative structure

The federated model, where a number of first-tier cooperatives own a second-tier cooperative has been accused of being obsolete (see next section). In the Mediterranean region the results are mixed. In some cases federated cooperatives have been very successful while in other sectors and/or regions this is not the case. It means that the connection between efficiency and single or multiple-tier cooperatives cannot be established. As the federated cooperative's main purpose is to overcome scale-problems in primary cooperatives, it means that those are too small for efficiently performing particular processing and marketing activities, but they can make sense in terms of facilitating membership involvement at the local or regional basis. By applying the subsidiarity principle federated cooperatives are able to benefit both from scale economies at the second-tier level and from strong incentives and low bureaucracy costs at the primary level.

On size and performance

Size is not the determining factor in cooperative success; good management is! The introduction of professional management is an important prerequisite for strengthening the market-orientation and competitiveness of cooperatives.

One of the recurring observations during the case study research was that the size of a cooperative is not a good predictor of its success. That is, both large and small cooperative firms have been successful in the Mediterranean and in the rest of Europe. The optimal size of a cooperative depends on the structural characteristics of the industry in which it operates and the strategy it pursues. In some cases, a large productive capacity is necessary for entering the industry (and thus might act as a barrier to entry). Yet, this is not the case in many other industries and regions.

Hiring professional management is crucially important for a cooperative's success. Cooperatives in southern EU countries seem to be in more urgent need of professional managerial skills. However, hiring professional managers also requires improving the skills of the board of directors. In order to avoid increasing agency costs due to a lack of oversight, cooperatives need to train their board members so that they can monitor management effectively and efficiently.

Mergers and collaborations among cooperatives

Horizontal collaboration (including mergers) among cooperatives can greatly support the performance of the individual cooperatives involved.

In most cases, collaboration between cooperatives has a strong positive impact on the economic performance of participating organisations, for instance in terms of accessing foreign markets, improving product portfolios, and enhancing the processing and distribution efficiency. A good example of this is the strategic alliance between the Spanish fruit and vegetables cooperative UNICA and its Dutch counterpart, ZON Fruit & Vegetables. On the other hand, collaborations between cooperatives and IOFs do not always have a similar effect (see above). Moreover, consolidation of cooperatives in some of the cases examined is imperative when benefitting from scale and scope economies is needed to maintain or improve competitiveness.

Overall conclusion

The classical quote from Alfred Chandler (1962) that “Structure follows Strategy” still holds for cooperatives, too. It means that firms that pursue a new strategy, such as a more consumer-oriented or more export-oriented strategy, need to adjust their structure. Strategy, in this context, is the central, integrated, externally oriented concept of what a cooperative wants to achieve and how it wants to obtain its objectives (i.e., what paths to follow and what resources to deploy). Structures, rewards, processes, people hired, activities, and functional policies and profiles are supporting organisational arrangements. The particular choices made by a cooperative are informed by the strategic analyses conducted, including industry, competitor, environmental trends, and an assessment of the cooperative’s internal strengths, weaknesses, and available resources.

The Santo Wine Cooperative in Santorini, Greece, is an example of the well-developed links and relationships between strategy and structure. Santo is a successful, vertically integrated, second-tier cooperative. Its product portfolio includes a wide variety of wines as well as other high-quality local food products. By assuming a competitive yardstick role, the cooperative has successfully supported and stabilised the income of its farmer-members who bypass their local, first-tier cooperatives and patronise directly Santo. In the past the federated structure was an efficient means of coordinating the wine supply chain on the island of Santorini. However, improvements in transportation, storage facilities and technologies adopted over the last decades have made the federated structure obsolete. In addition, Santo has decided to collaborate with IOFs as the most efficient strategy to reach the national and international markets. The key drivers of Santo’s success include its vertically integrated business organisation and the dominant position the cooperative holds in the local wine supply chain due to its mandatory status.

From the case studies in the Mediterranean F&V sector we also conclude that the establishment of producer organisations that control a significant part of the F&V trade at the local, regional or national level, has resulted in a more balanced distribution of bargaining power between producers and their downstream partners.

6.4 Federated cooperative structures

The federated model, where a number of first-tier cooperatives own a second-tier (or federated) cooperative, has been accused of being obsolete. Several empirical studies have shown that there is an international trend towards restructuring of federated cooperatives into single-tier cooperatives. In other cases the federated cooperative starts to employ activities far away from the farm products of its owners (see for example BayWa or the Dutch former cooperative Cebeco).

There are many federated cooperatives in Europe that provide important services to their first-tier member cooperatives and thereby to the farmers that are member of the first-tier cooperatives. When local or regional cooperatives are too small to make large-scale investments in processing or marketing, collaboration with other cooperatives in a federated structure can be an efficient means of achieving scale economies.

Federated cooperatives can be found in almost all agricultural sectors in the EU. However, when the first-tier cooperatives grow in size, often a merger process takes place between the first and second-tier cooperatives. Based on experiences with federated structures in Denmark, Soegaard (1994) has described three options for going from a federated to a unitary organisation: (1) the central organisation acquires (or merges with) the member organisations; (2) the largest member organisation takes over the central organisation; and (3) several large member organisations take over parts of the activities/assets of the central organisation, thus leading to several unitary organisations. Such structural change is not only a matter of growth to exploit economies of scale, but also a matter of change in the distribution of inter-organisational power. Soegaard suggests that there is a strong tendency for the balance of power in federative organisations to tilt in favour of the initially strongest member(s) of the organisation. The strongest member(s) will eventually use their power to force a restructuring towards a unitary organisation.

When such an integration of first and second-tier cooperatives is difficult for technical or political reasons, problems may occur. Unsuccessful cases of a federated structure are often related to governance problems due to increasing heterogeneity of the membership. The history of the Dutch multipurpose cooperative Cebeco shows that federated cooperatives may have a life cycle and that they may come to the end of their functional life when the first-tier cooperatives become so large that they do not need the second-tier cooperative any more.

In the Cebeco case, there was a mismatch and divergence of interests between large member cooperatives and the federated cooperative. Initially, the Cebeco Group had a positive track record on supply chain investments, created trust among members, but the member cooperatives no longer appreciated the diversification strategy. What we learn from the Cebeco case and has been described in the literature is that second-tier cooperatives have a lifecycle. The function of the federated cooperative may be gradually taken over by the primary member cooperatives.

Federated or second-tier cooperatives are not necessarily less efficient than first-tier ones. The case studies in this project provide mixed results; in some cases federated cooperatives have been very successful while in other sectors and/or regions this is not the case. The long-run trend, however, seems to be that the federated cooperative model is disappearing.

6.5 Bargaining associations

A basic function of any marketing cooperative is negotiating with customers. However, within the family of different types of producer organisations, specialised bargaining cooperatives or bargaining associations can be distinguished. Bargaining associations are set up by farmers to collectively negotiate a good price for their products and favourable delivery conditions. The counterparts in this negotiation process are usually processing companies, but they can also be traders, wholesalers or retailers.

There is a distinction between the bargaining association and the bargaining cooperative. While the bargaining association has a focus on negotiating, a cooperative often has more functions, for which it also has acquired particular assets. Thus, a cooperative is a type of firm, while the bargaining association is a type of association. The distinction, however, is not always clear cut, neither in practice, nor in legal form. The association will often not become the owner of the product that the farmers sell, where one might expect the cooperative to become the owner. However, there are examples where also the cooperative does not become the owner.

Most of the literature on bargaining associations has been based on the North American context, and mostly on the fruit and vegetable (F&V) industry (Iliopoulos, 2004). In F&Vs, a large number of bargaining associations exist because a substantial part of the harvest goes into processing. Processing companies are often IOFs. As there are substantial economies of scale involved in processing and marketing F&V, any processor has multiple suppliers of raw material. These supplying farmers are then organised in groups, in the USA often called agricultural bargaining cooperatives (ABCs).

ABCs are farmer-owned, farmer-controlled, and farmer-benefited associations that

negotiate terms of trade with processors-buyers of their raw product. Bargaining associations usually do not become involved with the handling of raw product and thus differ from marketing cooperatives (Hansmann, 1996). The literature identified two types of ABCs in North America (Marcus and Frederick, 1994). The first establishes minimum prices and terms of sale for their members' produce that must be incorporated in the contracts the members themselves execute for the sale of their produce. The second type, in addition to establishing price and terms of trade of sale, also acts as exclusive sales agent for their members and contracts for the sales of members' produce.

In most industries with effective bargaining associations, one or more processing cooperatives are also active. In some cases the processing cooperative evolved as a separate from, or next to, bargaining associations. In other instances, the bargaining association played a key role in the formation and organisation of the processing cooperative. It is not uncommon to find cases where the local IOF monopsony¹⁸ processor went out of business and the members of the ABC, or some of them, decided to buy the processing plant and operate it as a processing cooperative. The young Dutch dairy cooperative DeltaMilk is an example of this development.

The primary goal of a bargaining association is to obtain better prices and delivery conditions in market situations that are characterised by asymmetric market power (Ladd, 1964; Helmberger and Hoos, 1965). However, other explanations for the existence of bargaining associations have been put forward, like deterring post-contractual opportunistic behaviour by producers and processors operating under forward contracts (Knoeber, 1983; Knoeber and Baumer, 1986); enable price discovery in markets where there is uncertainty about supply and demand conditions (Hueth and Marcoul, 2006); and ameliorate moral hazard and adverse selection problems when quality grading is a difficult and costly process (Bogetoft and Olesen, 2004). Next to bargaining, these associations also facilitate efficient coordination of transactions between farmers and processors, by providing (or organising the provision) of services to its members like technical assistance, input supply, information exchange and arranging harvest and transport support (Bogetoft and Olesen, 2004).

One of the largest challenges to the success and sustainability of the bargaining association is the free rider problem (Helmberger and Hoos, 1965, Hansmann, 1996). Two types of free rider problems exist, one internal and the other external. The external free rider problem is most known, and it refers to the situation where a non-member receives benefits associated with the provision of public goods by the association (e.g., higher product prices), but avoids becoming a member—and thus eschews contributing to the costs associated with this provision. The internal free rider problem refers to the situation where some members do not fully comply with quality requirements, for instance when these requirements need specialised investments, thereby gaining individual rents but increasing group risk because it jeopardises the quality reputation of the whole organisation. This free rider problem appears in situations where individual compliance to quality requirements is difficult or costly to establish, such as in the case of using organic cultivation methods. While solving external free rider problem requires a facilitating legal framework, it also depends on the quality of solutions implemented by individual organisations.

From the perspective of competition law, a bargaining association is not always allowed, depending on the share of the market they hold or the impact of the association has on the efficiency in the food chain. The joint selling agreement by a bargaining association may constitute anti-competitive collusion, unless the agreement produces efficiencies for their members' production and distribution, so as to offset the restriction of competition due to the fixing of prices.

The processed F&V and the dairy industries are the sectors where most bargaining associations exist, although they can also be found in sugar and other crops that go into large-scale processing. The analysis below is based on case studies on POs in the Belgium processed F&V industry, the fresh F&V industry in The Netherlands and Belgium, and the Dutch and German dairy sectors.

¹⁸ A monopsony is a market structure in which many sellers face only one buyer.

Dairy

In the dairy industry, bargaining associations have existed for a long time. Particularly dairy farmers selling to an IOF processor often set up an association to bargain collectively with processors. Sometimes producers of specialty milk, e.g., organic milk, form an association, regardless of whether they sell to an IOF or to a cooperative. When the producers are also members of the processing cooperative, the association mostly has a (technical) coordination function. It provides its members with technical assistance and exchanges information between the specialty producers and the cooperative.

A rise in the number of dairy bargaining associations occurred in 2007, when suddenly milk prices increased rapidly and cooperatives did not immediately translate higher market prices into higher producer prices. In the Netherlands, a number of dairy farmers left their cooperative and started a new bargaining association to benefit from the growing demand for raw milk. The customers of these bargaining associations were processing IOFs, trading companies, or even cooperatives that needed more milk to operate at optimal processing capacity.

An interesting case of a new dairy bargaining association in the Netherlands is DeltaMilk. It was established in 2003 for collective purchasing of farm inputs. Then, when milk prices suddenly increased in 2007, it also became a bargaining association in the output market, jointly selling the milk of more than 100 members. In 2009, DeltaMilk became a dairy processing cooperative when it bought a cheese factory from the merged cooperative FrieslandCampina, which had to divest this factory in order to get EU approval for its merger.

Some bargaining associations in the dairy industry have a broader objective, i.e. lobbying policy makers concerning future dairy policies. Examples include the MEG Milchboard in Germany and the Dutch Dairymen Board. The European umbrella organisation, the European Milk Board, brings together bargaining and lobbying associations from almost all EU Member States. At the EU level, the purpose of these organisations is clearly lobbying for more favourable dairy market policies. At the national level, some of these organisations also function as bargaining associations, both towards IOFs and cooperatives.

Important reasons for dairy farmers to establish these new associations are both the strategies of dairy cooperatives and the EU dairy policies. These producer bargaining organisations represent a response to the dairy farmers' perception of loss of control over their cooperatives in the on-going race to increase size. At the same time, farmers face an increasingly liberalised dairy market with more volatile milk prices and increasing concentration in the food retail sector. The latter has resulted in strong bargaining power of just a handful of purchasing groups.

In this market situation, farmers experiment with organising themselves in bargaining associations, but at the same time resist to withdraw membership from large processing cooperatives because they feel the need to secure their delivery rights in times of quota abolition. Although (some) farmers have the feeling that they lost control over the large, customer-oriented dairy cooperative, they do not give up membership as they want to maintain their ownership rights, which have been build up over many years and which amounts to a substantial amount of capital, even in case these rights are not individualised. In this situation where farmers continue to be members of the large processing cooperatives, it is not clear what the role of the new producer organisations should be. While dairy farmers may be dissatisfied with their cooperatives, they still need them because only the cooperative can develop sufficient countervailing power in a highly concentrated retail market. It also means that for the moment there is not necessarily a conflict of interest between bargaining associations that are more interested in the short term objective of high prices, and the large cooperatives that continue to invest in innovation and marketing as part of a strategy to appropriate a part of the value added in the food chain.

Fruit and Vegetables

Bargaining associations are also set up by members of F&V cooperatives when they perceive a lack of control over their cooperative. Not the large size of the cooperative is the main reason for this perception, but rather its differentiation strategies and the heterogeneity of member

interests. The adoption of a vertical integration strategy is more likely to lead to the establishment of bargaining associations within cooperatives, as the member may perceive a stronger customer-orientation as a loss of member-orientation. Technical groups, often formed to represent the special interests of producers of one specific group of products in multi-product cooperatives, are not necessarily transformed into bargaining associations. Yet, if growers feel the need to start a bargaining association, such groups provide an initial organisational basis. The CMO for F&V has for a long time facilitated the development of more bargaining associations, particularly in countries where most of the subsidies are used for investments by individual producers or small producer groups, instead of investments at the level of the cooperative itself.

Recent policy reforms have put more emphasis on horizontal integration into larger POs, such as Associations of Producer Organisations (APOs). One of the main reasons for POs to collaborate in APOs is the concentration in the retail. The European retail market is dominated by approximately 15 retail purchasing groups, while there are hundreds of POs. The CMO for F&V has also facilitated the collaboration of national POs into international APOs. The improved information exchange within such international collaborative organisation provides the participating POs with better bargaining power and enables them to improve the efficiency of their R&D and logistic activities.

An example of international collaboration of POs in an international APO is shown in the case of the European Fruit Co-operation (EFC), a collaboration among three fruit cooperatives from Belgium, Germany and The Netherlands. EFC has shown that joint development and marketing of new apple varieties can deliver improved bargaining power and thereby higher prices for growers. The member POs established this international collaboration because also their retail customers operate on an international scale. Another advantage of the collaboration in EFC is the possibility to share the cost for developing and marketing new varieties. Having full control over the (year-round) production of new fruit varieties requires a scale of operation that goes beyond the scale of the member cooperatives of EFC.

The process towards larger organisations, although desirable from a countervailing power perspective, is often difficult as individual cooperatives have to give up part of their autonomy. At the same time, more traditional forms of collaboration among cooperatives are increasingly scrutinized by national competition authorities who in some cases appear to consider collaboration among independent cooperatives as potential collusive behaviour.

6.6 Dairy cooperatives as price setters

Cooperatives provide their members with market access and bargaining power. The latter is especially important in markets characterized by monopsonistic or oligopsonistic structures.¹⁹ By bulking the produce of many (small) producers into one offer, and negotiating about price and delivery conditions, cooperatives are able to establish countervailing power.

Our study found that in countries where dairy cooperatives have a large market share, farmers receive a higher milk price than in countries where cooperatives cover a small share of the dairy market. This result is based on an econometric analysis of different sets of milk price data (2008-2010, from Eurostat, LTO, EMB). Moving from a cooperative market share below 20% (the reference category) to a share of 20–50%, increases the milk price by roughly 4.5 to about 6 Euros per 100 kg – a relative increase of more than 15%. A further increase in the market share of cooperatives beyond 50% then slightly decreases prices, but price levels remain well above the reference category. Depending on the particular model (we estimated four different models), farmers still receive 2.5 to 4.5 Euros more for 100 kg milk compared to countries where cooperatives are minor players in the dairy industry.

These findings invite the question whether cooperatives generally pay a higher price to their members than IOFs pay to their farmer-suppliers. The answer is negative. We found that

¹⁹ While monopsony is a market structure with many sellers and one buyer, an oligopsony is a market structure with many sellers and few buyers.

the dairies in our sample on average pay below the country price. In 372 of 498 (about 75%) of the observations the price difference is negative. When standardised by the country average, cooperatives pay about 3 Euros less than IOFs per 100 kg of milk. Assuming a milk price of 30 Euros/100 kg this is ten per cent less – a substantial amount.

It seems that an overall strong cooperative sector increases prices while at the same time the cooperatives may not pay higher prices than their IOF competitors. In fact, in the two EU-wide datasets provided by EMB and LTO, we found that cooperative dairies on average pay less than IOF dairies – in all studied periods except 2011. Partly, these lower prices may be explained by the differences in contracts. As mentioned earlier, farmers usually sell all their produce to the cooperative, whereas IOFs often buy fixed contracted amounts. It may thus either be the case that IOF dairies have to pay a premium for not buying all milk and/or using fixed term contracts, or that cooperatives have higher costs because they have to process part of their milk deliveries into low value-added products. From our limited data it is difficult to conclude which of the two effects is larger. If, as we estimate, a strong cooperative dairy sector increases milk prices by 2.5–6 Euros this effect would dominate the lower prices by individual cooperatives. Western European dairies in our sample pay about three Euros less than their IOF competitors. Thus, in most cases a net benefit would remain for farmers in countries with strong cooperatives. Ironically, at the European level, the largest benefit of a strong cooperative sector accrues to farmers that supply IOF dairies. Thus, the high market share of cooperatives has a positive external effect on other producers. These findings are very much in line with the competitive yardstick theory.

Volatility

The EU dairy market has integrated the New Member States in the last decade. Over the last ten years, the fluctuation in prices seems to have had very similar patterns, both in timing and magnitude everywhere in EU. On-going price liberalisation seems to have tied the EU dairy market closer to the world market which faces problems of increased volatility.

In an econometric analysis, we found a price-variation-reducing effect of the market share of cooperatives (Figure 6.3). In addition we could show how the issue of being a New Member State still affected price fluctuation and that a regional difference between the north and the south of Europe in terms of volatility existed with slightly lower volatilities in the South.

A further exploration of differences in price volatility down to the firm level is difficult, given the differences in data availability between the EU Member States in general and between cooperative and IOFs in particular; this explorative analysis clearly pushed quantitative analysis to its limits. An analysis of data from Germany, Europe's largest dairy producer, revealed that general volatility over time was much larger than volatility between different types of firms. In terms of the volatility of prices paid to producers we found that no substantial difference existed between cooperatives and IOFs, even though, on average, prices paid by cooperatives were a little more volatile. We also found an effect of region on volatility, which, for Germany, can be attributed to the different farm structures between south and north and the proximity of southern dairies to neighbouring countries like Italy which due to different product orientation are known to have relatively higher and stable milk prices.

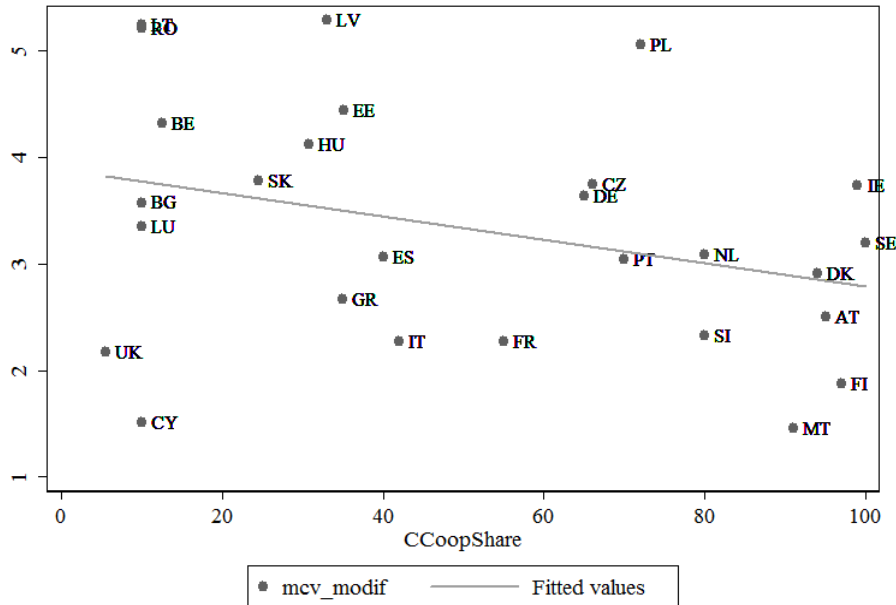


Figure 6.3. Cooperative market share and price fluctuation in average

6.7 Finance and access to risk capital

Finance is an often discussed topic in the cooperative literature. One recurring issue is the use of unallocated capital versus individual equity contributions by members, an issue also linked to internal governance (see above). Another matter is linked to horizon and portfolio²⁰ problems that may lead to lower investments by farmers than optimal.

In the case studies conducted we have seen many cooperatives where access to finance was not a major barrier to growth. Where profitable business opportunities exist, farmers are, in general, willing to invest. Although, on average, returns on investments in the first processing stage of the supply chain are relatively low (leading some IOFs to exit an industry), they are on average higher than in farming. In case of attractive business strategies, debt financing by banks is then available, sometimes there is even access to risk capital, by having co-investors (via stock markets or otherwise) in subsidiaries. This leads to hybrid cooperatives.

In cases where farmers own quite some assets (e.g., land) they seem to be willing to provide the cooperative with inexpensive capital that cannot always be invested profitably in the farm (and farmers do not want to invest outside the sector). This makes it possible for cooperatives to outperform IOFs, especially in older industries, where stock-listed IOFs have high opportunity costs.

The way cooperatives are treated by the tax authorities of most, if not all, Member States, seems to facilitate their growth. Cooperatives are treated as an extension of members' farms. Consequently, surpluses (money earned from selling members' products) return to members in cash or held in individual accounts by the cooperative are taxed only at the farmer level (single taxation principle). Profits, that is, money earned from selling non-members' products, are taxed at both the cooperative and farmer levels (the latter only if distributed to members), as happens with the profits of IOFs. In some countries, even cooperatives' profits are not taxed if they are kept in special reserves (e.g., for investments in R&D or education). Such provisions are particularly helpful for new and growing cooperatives but not of much relevance for larger cooperatives that conduct significant transactions with non-members. In some countries, the

²⁰ The fact that older members without a successor are not very interested in investing as they will not reap the rewards and the fact that farmers have a portfolio of opportunities to invest in, with some having a high opportunity cost when they are heavily indebted or can earn a high return on investment by marginal enlargement of their farm.

taxation of cooperatives is under discussion (e.g., in Spain, where the focus is on clarifying the types of cooperative capital).

This rather positive picture on finance of cooperatives' capitalisation is especially valid for regions with an efficient capital market. Several regions are an exception to this. There are clear cases where poor farmers operate in inefficient and incomplete capital markets without specialised banks that possess know-how on cooperatives, and without access to short-term credit. Access to risk capital and other forms of equity is one (but not the only) of the constraints facing cooperatives in Mediterranean countries, not permitting them to become niche cooperatives with better access to consumer markets (see above). As reported in some cases in Poland and Hungary, sometimes also the cooperative lacks the financial know-how.

In some cases farmers prefer cooperatives because they guarantee clear and known terms of transactions. We have also studied at least one case where this guarantee brought about severe problems for the growth of the cooperative itself.

7 International and transnational cooperatives

7.1 Introduction

In addition to the previous chapter on the position of cooperatives in the food chain, there are good reasons for an EU-wide study to pay special attention to the internationalisation of cooperatives. Internationalisation has become an important trend in the last decade. As in several countries the merger process within some sectors has more or less been completed, resulting in “national champions”, and European food processing companies are still small compared to the retailers as well as the American food companies (Wijnands et al, 2007), more international consolidation can be expected. Of course, this is also of special interest to the European Commission which commissioned this study.

The picture of transnational and international cooperatives (respectively cooperatives with foreign members and cooperatives with foreign farmer suppliers not being members) is rather complex. Many of the largest agricultural cooperatives in the EU pursue their economic activities through a separate legal entity. This cooperatively-owned firm may function in its international operations just like an IOF. This raises the interesting question whether the cooperative follows a different strategy in its host country compared to the home country, and whether it develops other supplier relationships in its host country (with non-member suppliers) compared to the home country (with suppliers who are members).

In addition, there are IOFs that are owned by first-tier or second-tier cooperatives from different EU Member States. This can result in a rather complicated structure: farmers are member of a domestic cooperative; this cooperative has formed a higher-level cooperative together with other cooperatives from other Member States; this higher-level cooperative is the holding for several IOFs; the IOFs source their products in different countries from different farmer-suppliers, only some of which are members of domestic cooperatives.

The next section looks to the motives behind and options for internationalisation. Section 7.3 provides data on transnationals and their strategies. Section 7.4 presents a case study on the sugar industry that shows how internationalisation is linked to strategy and internal governance.

7.2 Internationalisation of cooperatives

Foreign direct investment is a typical growth strategy. If growth opportunities inside a country are scarce because the market is saturated or because competition rules prohibit acquisitions and mergers, a company may seek expansion abroad. This happens sooner for companies in a small country like the Netherlands and Denmark than for their counterparts in larger countries like Germany or France.

Internationalisation can assume a variety of forms: export of products, issuing a licence for knowledge or a brand, and foreign investments in production. In the case of the latter, a firm can opt for a joint venture with another enterprise, a takeover of an existing factory, or setting up a completely new company (a greenfield investment). The choice of internationalisation strategy depends to a large extent on the nature of the company and the products. Small firms are more likely to opt for exports because foreign investments entail substantial costs and risks. Producers of voluminous and heavy products will be more likely to opt for production abroad because of the transport costs involved.

Beside the limited opportunities for growth in the home country, there are other factors which lead food producers to operate on an increasingly international scale. A first reason for a further increase in scale and internationalisation is the liberalisation of the European and world markets as well as the integration of the European market (and the introduction of the euro) and the increased competition that has resulted from this liberalisation. A second reason is connected with the structural changes in the retail of food products. In particular, the concentration among food retailers has led to an important change in competition dynamics.

Food companies can strengthen their competitiveness by following the internationalisation of retail companies. A third reason for internationalisation is consumer demand for more variation, more convenience and higher quality. Not only has the quality of the final product mattered, but also animal welfare and the environmental impact of the production process. This obliges producers to make greater efforts in the field of product development, quality control and marketing. The required investments call for a larger, often international scale of operations.

Cooperatives in the food chain pursue internationalisation strategies just as their IOF-competitors do. Cooperatives can choose export, licensing and foreign direct investments. However, cooperatives also have another option for internationalisation: they can become a transnational cooperative by having members in more than one country.

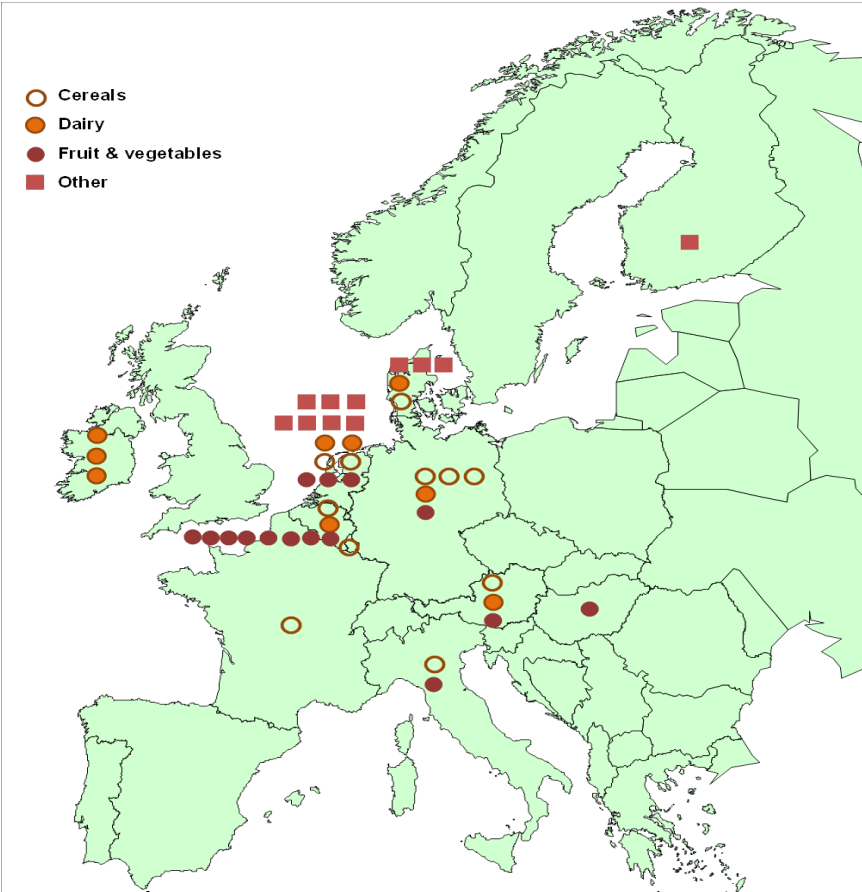


Figure 7.1 Transnationals by sector and mother country

Research focusing on the internationalisation of cooperative membership does not exist; only some anecdotal evidence has been presented. For instance, Van Bekkum and Van Dijk (1997) mention a number of examples of transnational cooperatives in the Netherlands, Germany, Belgium and Luxemburg. Bijman and Van Tulder (1999) discuss several Dutch cooperatives that internationalised in the 1990s by obtaining foreign members.

The number of transnational cooperatives in the EU has grown over the last decade. However, our research has shown that few cooperatives opt for an internationalisation of their membership. Transnational cooperatives can only be found in a limited number of sectors and a limited number of countries (Figure 7.1). Mostly, they are found in dairy and fruit & vegetables, and in the following Member States: Belgium, Netherlands, Germany, Denmark, Sweden and Finland. Thus, transnational cooperatives are mainly a northwest European phenomenon.

7.3 Transnational cooperatives

We found only 46 transnational cooperatives of which some are federated. Many of these transnational cooperatives act also as international cooperatives, i.e., they have farmer suppliers in countries where they do not have members. Furthermore, we found 45 international cooperatives, i.e., they have farmer suppliers in foreign countries (this excludes some cooperatives that have a few members just across the border). In addition to these, there are of course many cooperatives that have export activities but these cooperatives are not been analysed in this chapter.

Table 7.1 presents the number of transnational and international cooperatives in EU in the different sectors. The main sectors with transnational cooperatives are cereals (often also input suppliers at least of compound feed), fruit and vegetables (F&V), and dairy. The other sectors where there are transnational cooperatives are meat (pig meat, cattle and poultry in one cooperative), eggs, genetics, potatoes, and input supply.

Table 7.1. The number of transnational and international cooperatives by sector

	Transnationals 1 (members in all supplying countries)	Transnationals 2 (members in some but not all supplying countries)	Internationals (members only in one country and suppliers in other countries)
Cereals (usually also input supply)	4	7	7
Fruits and vegetables	12	3	15
Dairy	6	3	8
Sugar	2	0	3
Other sectors	8	1	12
Total	32	14	45

How do cooperatives become transnational? Nilsson and Madsen (2007) list four different strategies that cooperatives can follow to become transnationals. First, a national cooperative can recruit members in a neighbouring country. Second, a cooperative can acquire a foreign company and then invite the suppliers of the acquired company to become members. Third, farmers from different countries can establish a new transnational cooperative. Fourth, a cooperative from one country may merge with a cooperative from another country.

Strategy 1: Recruiting members from a neighbouring country may happen where scale economies in processing and/or marketing are important and the cooperative needs to tie foreign producers to its own processing and marketing activities. It is not uncommon for farmers living in border regions to be members of a foreign cooperative, particularly when countries share similar cultural characteristics (particularly language). The distance to the foreign cooperative may be smaller than to a domestic one. Such cross-border membership can be found between Belgium and the Netherlands.

Particularly in the F&V sectors of Belgium and the Netherlands there are quite some transnational cooperatives. While Dutch F&V cooperatives have several foreign members, most of the international membership can be found among Belgium F&V cooperatives. The Belgian fresh F&V cooperatives continue to use an auction clock for price determination. This sales method has attracted quite a number of producers from The Netherlands, but also several from France and Germany (Table 7.2). As auction cooperatives need to attract as many buyers as possible (to maintain competition in buying), they are keen on having a broad product portfolio and having sufficient quantities available. Thus, it is attractive for auction cooperatives to invite foreign producers to become members. Next to the 868 foreign growers that were members of Belgian F&V cooperatives, some 100 Belgian growers were members of Dutch cooperatives (Vlaamse Overheid, 2008/2011: 93).

Table 7.2. Foreign members of Belgian F&V cooperative (2007)

Country of origin	Number of growers
Netherlands	637
Germany	34
France	197
Total	868

Source: Vlaamse Overheid, 2008/2011: 93

Strategy 2: Acquiring a foreign IOF processing company rarely leads to a transnational cooperative. The suppliers of the foreign IOF may continue to supply the new owner, but seldom are they invited to become members of that new owner. Exceptions have been found in the potato starch and dairy industry. When the Dutch potato starch cooperative Avebe acquired a potato starch company Prignitz Stärke GmbH in Germany in 1995 it invited the suppliers of this company to become members of Avebe. Due to the bilateral dependency between starch potato growers and the processor, and an EU quota system for starch potato production, membership of the processing cooperative is the favourable means of reducing transaction costs.

Cooperatives may also acquire all assets of a foreign cooperative, and then invite the members of that foreign cooperative to become members of the acquiring organisation. A pure case is the 1999 acquisition by Austrian dairy cooperative Berglandmilch of all assets of the German dairy cooperative Rottal Milchquell eG. The members of Rottal Milchquell became members of the Austrian cooperative Berglandmilch. In 1997, Dutch dairy cooperative Campina entered into a joint venture with the German cooperative Molkerei Köln-Wuppertal (MKW). Soon after that, the members of MKW were invited to become members of Campina. Acquisition of the assets of a foreign cooperative instead of merging with that foreign cooperative is usually chosen when the foreign cooperative is in financial trouble, as a merger would not be accepted by the members of the acquiring cooperative.

Strategy 3: The establishment of a new transnational cooperative is a rather rare phenomenon. The only exceptions can be found in the F&V industry, where the availability of EU subsidies under the CMO regulation for F&V has supported the establishment of cross-border producer organisations (APOs). An example is EFC, the European Fruit Co-operation, which has been established in 2002 by three specialised fruit cooperatives: Veiling Haspengouw from Belgium, Württembergische Obst- und Gemüsegenossenschaft (WOG) Raiffeisen from Germany, and Koninklijke FruitmastersGroep from The Netherlands. As its members are the three national cooperatives, EFC is a second-tier cooperative. Other examples of transnational APOs in the F&V industry are In-Co (with member cooperatives in Netherlands and Belgium), and Vegras (with member cooperatives in Belgium, the Netherlands and France). All three are established in Belgium. While Vegras is a bargaining cooperative for growers supplying the processing industry, EFC and In-Co are handling fresh F&V. Finally, B.N.D. Internationale Telersvereniging is a transnational bargaining cooperative in the processed vegetables sector, established in Belgium and with growers from Belgium, Netherlands and Germany as direct members.

Strategy 4: Examples of transnational cooperatives through a cross-border mergers between two or more cooperatives can be found in the dairy industry (Figure 7.2). A prime example is Arla Foods, which is a result of the 2000 merger between the largest Danish dairy cooperative MD Foods and the largest Swedish one, Arla. After the merger, Arla Foods had more than 10,000 members, equally distributed over the two countries. After 2000, Arla Foods continues to seek international expansion through mergers. In 2003, a merger attempt with Dutch Campina did not succeed. However, other mergers continued, particularly with several small Swedish and Danish dairy cooperatives. Some of these mergers should be classified as acquisitions, as the acquired cooperative was in financial trouble and was “saved” by Arla Foods. In 2011, Arla merged with another foreign cooperative, Hansa Milch, from Germany. This latter merger was, similar to the domestic ones earlier, a merger of unequals. The turnover of Hansa Milch was only 5% of that of Arla Foods.

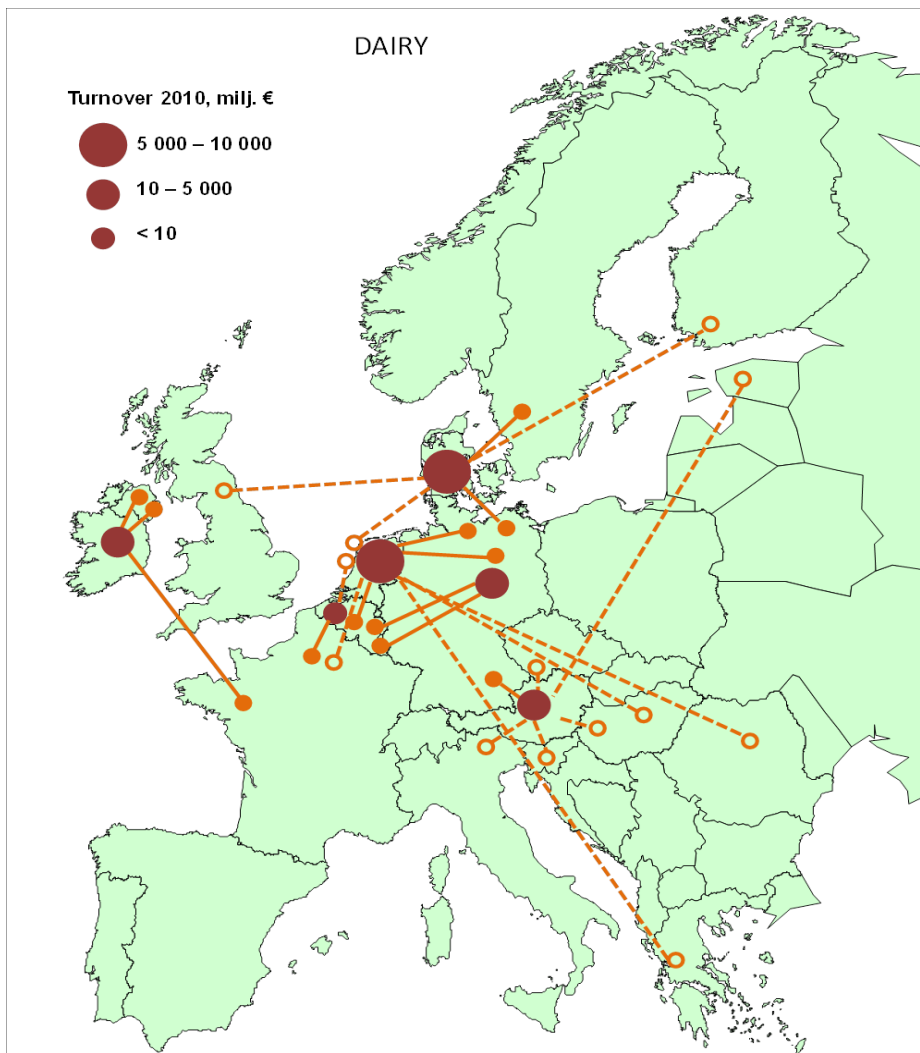


Figure 7. 2 Transnational cooperatives in dairy sector - mother countries and host countries (the solid line refer to the countries where there are member suppliers, the dotted line refers to countries where there are farmer suppliers but not members; the size of the “balls” represent the total turnover (in this sector) of the transnational in its mother country).

In 2012, Arla Foods announced that it had plans to merge with the German dairy cooperative Milch-Union Hocheifel (MUH) and the UK dairy cooperative Milk Link. If successful, these mergers will make Arla Food the most transnational cooperative in the EU, with 12,300 members in six different countries: Denmark, Sweden, Germany, Belgium, Luxembourg, and the UK.

In addition to the four types of transnationalisation processes distinguished by Nilsson and Madsen, we found transnational cooperatives that do not necessarily fit into these types. There are different kinds of federated (or semi-federative) structures that have been partly a result of acquisitions or cooperation with companies/cooperatives from different countries (e.g. Danish DLA, Austrian RWA, and German BayWa). These cooperatives are often involved in the input supply business where the ties between members’ supply and members’ usage of own cooperative services are not strong.

HKScan is an example of an international cooperative hybrid. By acquiring Scan AB, a processing company owned by the Swedish Meats cooperative, HKScan became a major meat producer in Sweden. However, the Swedish producers of meat did not become members of LSO, the main cooperative owner of HKScan. Swedish producers have become, through their

cooperative, co-owners of HKScan, but only of a small percentage. Thus, while HKScan is an very international company, its main owner cooperative continues to have only Finnish members.

Transnational or international cooperative?

The same cooperative may be structured as a transnational cooperative (i.e., suppliers are members) in one country and like an international cooperative (suppliers are not members) in another country. From our research into transnational and international cooperatives in the EU, it seems that the default option is internationalisation, not transnationalisation.

Already Nilsson and Madsen (2007) indicated that a cross-border merger of cooperatives is a much more complicated growth strategy than the acquisition of a foreign IOF. A cross-border merger between cooperatives actually involves two interdependent merger processes; one concerning the cooperative firms and the other concerning the cooperative societies. Thus, not only top-managers need to agree, but also the boards of directors, and ultimately the ordinary members (as most bylaws stipulate that merger decisions need approval of the General Assembly). Also, the implications for the existing members are far-reaching. Inviting suppliers in another country to become members has implications for decision-making and member-cooperative communications, particularly when members speak different languages. Another argument disfavouring transnational cooperatives is the dilution of member income. When the foreign activity is profitable, all profits are distributed to current members, who do not have to share them with foreign suppliers. Also in terms of ownership, inviting foreign suppliers to become members implies a dilution of wealth (assuming that foreign members do not bring in the same assets per member as the incumbent members, which is often the case).

Also managers prefer internationalisation to transnationalisation, as they want to run a foreign operation like an IOF and not like a cooperative. Running a foreign subsidiary is already difficult enough; running it while continuously taking into account the interests of the foreign members is even more difficult. We found that most cooperatives prefer to internationalise by acquiring or setting up foreign IOFs, and not by merging with other cooperatives. Dilution of ownership and control are cited as the main arguments by our interviewees.

In sum, the question why internationalizing cooperatives do not use the cooperative structure in host countries after acquiring foreign processing activities, can be answered as follows:

- It raises the costs of decision-making, due to differences in culture, in membership traditions, in language, etc.
- It dilutes the control rights of current members.
- It dilutes the income rights of current members.
- Managers prefer to run the foreign subsidiary as a profit centre (making monitoring and control of the foreign subsidiary easier).

It should be emphasised that a cooperative choosing the form of an international instead of a transnational cooperative when engaging with foreign suppliers does not necessarily mean that the cooperative is exploiting these foreign suppliers. It is in the interest of the acquiring cooperative to establish good relationships with its foreign suppliers, for instance to obtain good quality deliveries. Often the acquiring cooperative brings new knowledge to the supplying farmers. Also, supplying farmers may be encouraged to set up a producer association for sharing technical and managerial experiences.

7.4 Internationalisation in the sugar industry

In order to study firm-specific differences in internationalisation strategies, institutional differences, and member-company relationships, we conducted a separate case study on the internationalisation strategies of sugar cooperatives, comparing the German/Austrian hybrid cooperative Südzucker/AGRANA, the French cooperative Tereos and the Dutch cooperative Cosun.

In the sugar industry, producer organisations play an important role not only in supplying

the industry with sugar beets but also with respect to the internal governance of sugar firms and their strategic positioning. In this respect, our analysis identified differences between cooperatives. Cosun and Tereos are traditional cooperatives owned by sugar beet growers, most of them also growing potatoes, cereals and some field vegetables. Royal Cosun is a cooperative with 10,000 members, while Tereos is a cooperative with 12,000 members. The cooperatives have contracts with their members and voting rights are in proportion to member patronage. Compared to these two, Südzucker/Agrana AG is a public company listed at the stock exchange with a somewhat different business model. Due to historic decisions Südzucker can be characterised as a Cooperative-IOF, in which the producer cooperative (Süddeutsche Zuckerrübenverwertungs Genossenschaft eG [SZVG]) is the major shareholder that always tries to keep its majority at the level of +51% of the shares (but farmers are not the only members of SZVG). SZVG is not the founder of the firm. In all three cases members have direct influence on the policy and strategy of the cooperative through elected representatives who serve on the Members' Council.

The sugar beet farmers in the four countries had enjoyed substantial productivity gains over previous decades as the sugar beet production developed to a stable and profitable farming business for small and larger family farms. To assure the quality of the sugar beet delivered by its suppliers, the sugar companies provide technical support regarding the best sugar beet strains, soil preparation, and agricultural inputs. In addition to technical assistance, the sugar industry maintains a policy of financial incentives for suppliers. While the EU sugar regime established price ceilings, the sugar company organised (or negotiated with sugar beet grower unions affiliated to them) everyday business matters of remuneration of sugar deliveries and quality premiums, refunding of transportation costs, planting, and harvesting matters of the crop. There are nearly no differences in the attitude of the sugar firms towards their suppliers.

The sugar companies realised long ago that excellence in the field of sugar production required heavy investments in the farmer/member relationship to become supportive to their businesses. Great emphasis was placed on the staff that was devoted to advising farmers. Only good relationships, it was reasoned, could transfer the agronomic and market knowledge. Our findings suggest that there exists a mutually beneficial relationship between sugar growers as members and sugar firms. It is the cooperative character and the institutional partnership between producer organisations and sugar companies that matters when it comes to the annual negotiations on sugar prices and delivery conditions.

Despite all changes in the market conditions (EU sugar regime, competitive sugar substitutes, increase in sugar imports), all companies continued to invest in sugar production and technology improvement. Having played an instrumental role in the development of sugar production in their home countries all three companies trust their competitive advantage in sugar production. Although the companies were active across a broad spectrum of product groups, food and non-food industries and countries (except for Cosun who was concentrating its activities mainly in the national Dutch market), sugar production remained the cornerstone of their businesses (Südzucker's sugar production share remains at 53% and Tereos' at 43% of the total turnover).

After many years of relatively stable market and regulatory conditions, the industry as a whole had been under tremendous pressure to develop new competitive strategies as an answer to the upcoming changes in the regulatory framework. Since the 1990s, the European Union has made some important changes of the common sugar regime with special emphasis on sugar prices guaranteed to farmers and international trade liberalisation. The sugar industry expected the depressive effect on future sugar crops to seriously curtail demand for sugar beets in non-favourable regions in Europe and sugar cane imports from Brazil and the Caribbean would flood the market. The sugar industry reacted in different ways to these challenges:

- Consolidation of sugar production capacities through mergers and acquisitions in the domestic market (heavy merger activities by Südzucker and Tereos within the German resp. the French sugar sector; in the Netherlands the IOF CSM sold out to Cosun).
- Diversification of sugar processing activities and investments in sugar related value creation (ingredient processing, production of sugar substitutes) and in the extension of

scope activities by investing in other food activities. All three companies invested in several stages of the food chain or other sectors.

- Internationalisation of their activities in foreign sugar industries (Südzucker in neighbouring countries, like Belgium, France, Austria, and Poland, and Tereos in the Czech Republic, Cosun in the East of Germany).

The reforms of the sugar regime had an enormous impact on the restructuring of the sugar industry and on companies' strategies. In recent years, Cosun re-designed its strategy, focusing on sugar production, large-scale processing and adding value to vegetables and residual materials. As a consequence, Cosun sold business activities that were too far unrelated to sugar or vegetables. It is staying close to its members: arable farmers that grow sugar beet, potatoes, vegetables and cereals.

Südzucker and Tereos took different strategic decisions. They decided to invest in diversified business segments and get successfully access to different product markets (e.g., processed food, food ingredients, bio-energy). The Südzucker and the Tereos groups grew through horizontal and vertical diversification and integration. Tereos combines vertical integration and diversification strategies, insisting on this even more since the implementation of the EU sugar regime reform. This strategy is based on controlling the whole process from A to Z for sugar beet, sugar cane, cereals (wheat, maize, potatoes, and manioc). That is why the group has agreed to create more room for the transformation of cereals, via its subsidiary Syral. A difference with Cosun is that its farmers are more active in cereal production and more interested in bio-ethanol. The group has also diversified into starch-based products by acquiring five factories from the British Tate & Lyle group.

A number of industry-driven factors have prompted the two companies, Südzucker and Tereos, to develop such an international strategy. These factors include the growing homogeneity of demand, rising economies of scale, increasing technology intensity of new products, the pressure to amortise high costs of R&D, and proprietary investments into critical value-adding activities through diversification, e.g., food product production, food ingredients, etc. These industry drivers oblige the companies to compete along a highly standardised and consistent manner across different markets. The domestic and foreign markets the companies entered are highly interdependent and mutually supporting as far as sugar beet farming, sugar production, and marketing are concerned. Transfer of knowledge in these functions was easily possible and created a high level of internal cohesion and consistency. Key to pursuing an international strategy was the integrative view of building and extending their sources of competitive advantage. Both Südzucker and Tereos viewed each market in which they were competing as a platform to learn new skills and techniques that were then applied to other markets. This strategy also helped the firms to extend their distinctive competences to build leverage across markets. Going international, Cosun, Südzucker/Agrana, and Tereos do not apply their cooperative or semi-cooperative business model for the sugar beet growers in the new countries. They were considering the acquired companies as an additional business unit, which implied a purely contractual relationship between the company and its foreign grower-suppliers.

In conclusion, this case shows that cooperatives, at least with the support of market regulations, can contribute to a stable and continuous production, processing, distribution and marketing of food and non-food products and services, and to a (more) stable farmer income. The likelihood that farmers are willing to support cooperatives' investment policy by providing equity increases if a more profit oriented firm organisation is created. This governance structure then would necessarily deviate from the traditional cooperative model. The high cost of integrating foreign sugar beet suppliers into a cooperative membership system prevents the sugar cooperatives we analysed from choosing the cooperative business model when they were acquiring their foreign subsidiaries.

8 Institutional environment: historical, social and cultural aspects

8.1 Introduction

In all European countries, including transition countries, a shared cooperative tradition is observed, with the establishment of cooperatives in the 19th century and the experience of realising social and economic objectives (Chapter 3). However, we see important differences between Member States in the market share of cooperatives, even within the same sector (Chapter 4).

These differences in the performance of cooperatives might be partially explained by historical, social or cultural factors. This is most clear in the case of the New Member States, which have experienced a massive destructive impact of the totalitarian communism/socialism on self-organisation, trust and social capital and, as a result, the term “cooperative” has ended up having a negative connotation.

In this chapter, we first present an analysis of the relation between social and cultural aspects and cooperative performance, in an attempt to identify deeply rooted social or cultural values that block the success of cooperatives. That is followed in section 8.3 with a deeper institutional analysis of the situation in the New Member States. It shows how important the different (now historical) methods of privatisation in the post-1989 transition are for the current performance of cooperatives. We end with a section on human capital.

8.2 Social and cultural aspects

The literature on “social capital” provides numerous insights on how to facilitate corporation, the formation of networks and trust. In economics “social capital” is increasingly recognised and studied as an important factor for economic performance. However the concept, and especially its measurement, is still work-in-progress.

Social capital is generally defined as the trinity of “networks, norms of reciprocity and trust.” It refers to anything that facilitates individual or collective action, generated by networks of relationships, reciprocity, trust, and social norms. A certain circularity can be discerned: through social networks trust is developed, but trust is also needed in order to engage in networks. Likewise, the existence of social capital is often inferred from outcomes that are supposed to be the result of its existence. Moreover, social networks are not merely a positive thing: social networks can also have negative aspects, such as the exclusion of outsiders, anti-social objectives, or restriction of individual freedom and autonomy (e.g., mafia).

The measurement of social capital is still in its infancy. We therefore used a few separate components of social capital: the relationship between trust and the performance of cooperatives (measured in terms of the percentage of farmers in a country who are members) in terms of general trust (trust in other people), as well as trust in political institutions. In addition, we studied the relationship between the performance of cooperatives, the level of engagement in voluntary work, as well as the general feeling of satisfaction with life (a prerequisite for trust).

We found a clear correlation between the level of general trust (operationalized as “trust in people”), and cooperative performance (Figure 8.1). All New Member States (and Portugal) are in the bottom left corner with low trust and a relatively small role reserved for cooperatives. Most of the countries with a high market share for cooperatives are high-trust countries. Luxembourg and Sweden being outliers, can be partly explained by the fact that some of the cooperatives active in these countries are foreign (and membership was underestimated in our indicator).

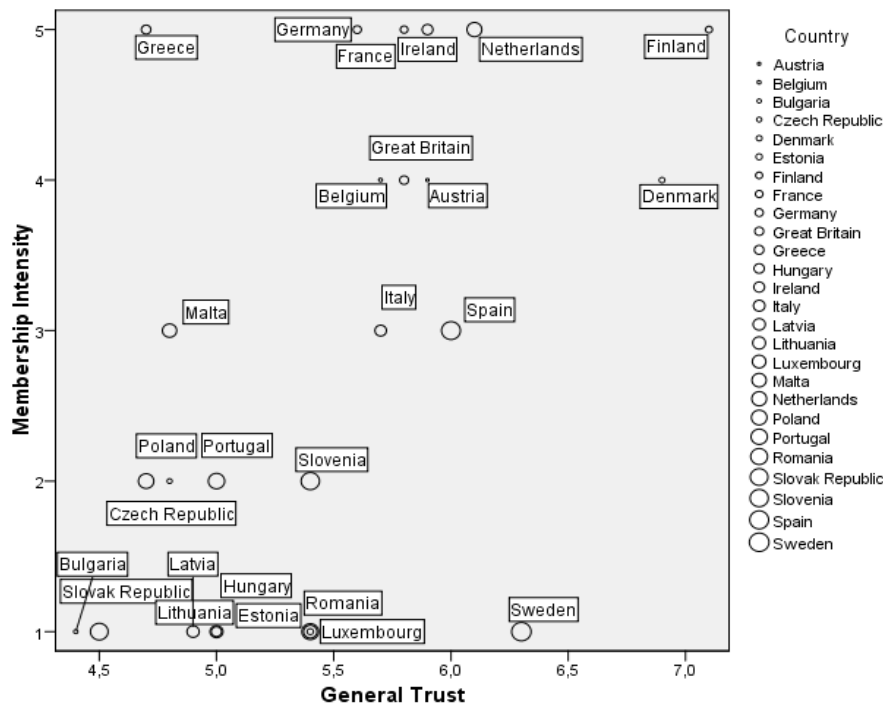


Figure 8.1. The relationship between trust and cooperative performance

We found similar results for the variables “trust in political institutions” and “life satisfaction.” The results for the variable “engagement in voluntary work” is even more striking: we find two clear-cut clusters, with Greece and Spain, where voluntary work is less frequent than in surrounding countries, being in between, as well as Slovenia where more voluntary work is not matched by cooperative performance. Cooperatives also represent social capital networks and act as loci of engagement in collective action, which is intended to produce potential benefits at the group level exceeding simple self-interest.

The aforementioned findings suggest that the poor performance of cooperatives in some countries (particularly New Member States) has an important social background. Low levels of self-organisation and networking have far more consequences for these countries than simply constraining cooperative development. The issue then, is how deeply rooted in culture are such characteristics and behaviours.

Cultural aspects

Deeply rooted cultural values remain relatively unaltered by modernisation or, to the extent that changes occur, these happen across all countries and, as a result, no change between countries takes place (Hofstede et al., 2010). Hofstede’s seminal work shows that national and regional cultures influence the behaviour of societies and organisations and that these influences are persistent over time. The values that distinguished countries (rather than individuals) from each other appeared to group themselves statistically into four clusters, referring to four anthropological problem areas that different national societies handle differently: ways of coping with inequality (Power Distance), ways of coping with uncertainty (Uncertainty Avoidance Index), the relationship of the individual with her or his primary group (Individualism versus Collectivism), and the emotional implications of having been born as a girl or as a boy (Masculinity versus Femininity). Two additional dimensions are related to the choice of focus for people’s efforts: the future or the present and past (Long- versus Short-Term Orientation) and to the extent of gratification of human desires for enjoying life (Indulgences versus Restraint).

We analysed the relationship between each of these six dimensions of culture and cooperative performance, as we did above for the social aspects. To cut the story short: we could not find any significant correlation. This is a striking result, seen the correlations above for social

aspects and the fact that the Hofstede indicators have otherwise correlations with many entrepreneurial and organisational aspects. This result might be explained by the overwhelming need for cooperation in the market (e.g., in some countries where cultural values are similar to those with minor cooperative activity) and with past experiences with highly instrumental, hybrid organisations.

This finding conveys promising news for those who want to promote self-organisation and cooperation in (New) Member States. Although constraining social factors do exist, the possibility of overcoming them is not negligible.

8.3 The effects of the transition history in the New Member States

Compared to other EU Member States, the social institutions and economic drivers, including relevant obstacles for sustainable cooperation in post-socialist societies, are quite different in Central and East European countries (Hagedorn and Eisen, 1998). The following aspects are particularly relevant (Hagedorn 2004; Beckmann and Hagedorn 2007):

- The historical development of agriculture and rural areas is diverse across the NMS.
- The evolution of cooperatives has been interrupted by the socialist era when self-organised cooperatives were replaced by collectives imposed by central planning.
- In particular, agricultural production collectives became a dominant type of farming; however, not in Poland and Slovenia where collectivisation failed.
- Privatisation, restitution and transformation laws designed after 1990 were rather diverse, which led to unequal transformation of collective farms into cooperatives.
- Similarly, diverse ownership structures on agricultural land existed due to differences in land reforms that occurred in the pre-collectivisation era.
- Both the diversity of the transformation process and differences in pre-collectivisation land ownership in the NMS had specific impact on the persistence and roles of agricultural production cooperatives and the emergence of new cooperatives.
- Cooperative laws and statutes differ and sometimes disregard cooperative principles.
- The NMS differ in social capital, trust and reciprocity being important preconditions for successful collective action, as well as regards a tradition in cooperatives.
- Livelihoods in rural areas differ considerably between the NMS due to unequal farm sizes, emergence of subsistence farms and even the degree of rural poverty.

In our case studies we investigated three issues:

- (1) Many cooperatives in the former socialist countries (including East Germany) are the transformed successors of the former socialist cooperatives (collective farms) that, of course, also sell their products. In this study we are especially interested in cooperatives active in downstream parts of the food chain. Such new cooperatives have been established in the NMS. As both successes and failures of such cooperatives can be observed, the question of what can make them sustainable arises. In addition, the establishment of new cooperatives in the NMS has been supported by EU and national policies. What has been the impact of these policies? What problems have the new, emerging cooperatives been facing and how can they be solved?
- (2) In several NMS, cooperatives are still providers of social services to rural communities and contribute to rural development. Agricultural production collectives in formerly socialist countries had assumed a variety of tasks which were fulfilled by municipalities, regional governments or NGOs in western countries. Which of these functions have been maintained by post-socialist cooperatives after the reforms? Which new activities have been developed such as environmental services or rural tourism?
- (3) Large agricultural producer cooperatives (APCs) in post socialist countries may have taken the lead in rural regions providing commercial services to other farmers and in some cases to communities. This leads to the questions: which basic commercial or social services do

they provide in rural areas? Could this be endangered by EU policy reforms? Experts from Central and Eastern European countries often highlight the importance of APCs for the development of markets. Will this continue in the future?

Starting from these research questions, two comparative case studies were conducted on each of the three topics. We report on these twin cases as they provide striking insights.

8.3.1 The twin cases Poland and Hungary: the role of trust-building leaderships

In Poland, similar to communist reforms in all Central and East European countries, the collectivisation and nationalisation of agriculture followed the Soviet pattern. However, collectivisation faced strong resistance from Polish farmers and failed after a few years. The family farm system was subjected to the system of central planning which did not allow for institutionalising dynamic labour, input, product and factor markets. Accordingly, the family farm structure in Poland was more or less frozen during the socialist era. As much as 25% of the Polish labour force was still employed in agriculture in 1990. In the formerly German territories of Poland, state farms were established and privatised after 1990 (Milczarek, 2002). The establishment of marketing cooperatives accounts for this dual structure of agriculture.

Based on a detailed analysis of three cooperatives²¹ (and earlier work in the country study) we conclude that policy support has been crucial for the emergence of new marketing cooperatives. Yet, policy support is considered a necessary but not sufficient condition. This observation is in contrast with the two Lithuanian cases where policy support was not applied for. In two of the Polish groups, farmers' cooperatives had existed before, and this cooperative tradition was still part of the collective memory in the regions. However, building a cooperative on this collective historic memory was severely hampered by the so-called "communist legacy", the problem of distrust in all types of cooperation. In the perception of many Polish people even the term is discredited due to the role that enforced collectives played during the socialist era.

As shown by the Polish case studies, overcoming this barrier has been in the first place the task of trustworthy and skilful leadership. This kind of leadership is the scarcest resource in the case and a real constraint to further development of cooperatives in Poland. It is striking that the leaders identified in the Polish cases combined different roles in one person, such as the social local leader, the board director, and the manager. They were brought up in the region and were familiar with the rural society and the specific social and economic environment.

Polish experiences stress (in line with some theory on the need of a "free actor" in such social processes, who is trusted as not pursuing only his own interests) the point that a professional organiser of the cooperative is required who is not a farmer and a member of the cooperative but an outsider with a good education, professional skills and sufficient motivation provided by means of adequate payment. In the initial phase, when the cooperative was established, overcoming distrust by direct communication was the core task of the leaders. This experience was also emphasised in the Lithuanian cases where building trust by communication that seriously paid attention to the concerns and problems of members played a crucial role. In other words, formation of cooperative groups requires leaders with social, economic and organisational skills that have sufficient time and capacity for crafting the institutions (sets of rules) of the cooperative in a bottom-up process.

However, even if this cooperative development process is successful, cooperatives will only become sustainable if their services are really needed by the farmers. For example, in the case of the Polish pig cooperative, farmers were facing unstable conditions typical of the pig market and expected their cooperatives to provide better market access and less price volatility. Meeting these expectations required the leader to have considerable strategic skills for the development of concepts and vision for the future, but also the ability of muddling through in difficult phases.

²¹ JAR-PEK: a pig meat production cooperative producer group, which includes eight producer groups that started as spin-offs; Sady Krajny: a fruit production group established by the support of a local cooperative bank and Krobica: a cooperative group of producers of fruits and vegetables specializing mostly in tomatoes delivered just to one company (Heinz).

For example, survival of at least one cooperative depended crucially on the possibility not only to spend public support on coordination but also on investments. Only after an intense bargaining process, the manager received this permit from the authorities.

In addition, formal skills are required as the manager has to cope with administrative requirements when applying for policy support, must be familiar with legal procedures, such as receiving a construction permit, must care for correct accounting of the cooperatives' transactions, etc. Farmers usually dislike such tasks (and are even reluctant to pay for them because they are not perceived as "real work" by traditional rural societies). Economising on these work processes enables the cooperative management to achieve comparative advantages vis-à-vis individual marketing.

The role of knowledge and education cannot be overemphasised, in this respect. Only leaders who have a good reputation and are trusted by their members can successfully enforce the rules of the producer group. They were even able to impose penalties in case of non-compliance, which is particularly important as regards the delivery obligation of members. Their capacity to prevent the failure of collective action is a prerequisite for the formation and sustainable development of a cooperative. Destructive behaviour of leaders such as elite capture did not play a role in the Polish cases. The same conclusion was drawn in the Hungarian cases where the issue of proper budgetary planning and financial continuity was even more important.

Another point emphasised was pursuing a vertical integration strategy to protect against international markets. As these cooperative are still vulnerable, a more continuous, instead of temporary, policy support is seen as necessary.

In summary, it can be concluded that particular emphasis on reliable, trustworthy and professional leadership played a predominant role in the Polish cases. However, this is a necessary but not a sufficient condition, as the establishment of cooperatives is only feasible with more than medium-term support by policy measures.

Hungary

Unlike what happened in Poland, collectivisation was completed in Hungary. However, Hungary developed its own way of organising collective farming, which typically was a symbiosis between the cooperative and the small private holdings of cooperative members. In addition, Hungary was an important exporter of agricultural products during the socialist era, even to the Soviet Union. The development of post-socialist agriculture in Hungary has been influenced accordingly by the choice of privatisation and transformation procedures. Since the Hungarian parliament decided for voucher privatisation, large farm units were not immediately abandoned (like in Bulgaria) but could be maintained by using the vouchers in auctions.

Although Hungary differs in this respect from Poland, similarities between the two cases do exist. Based on the country report and detailed investigations in three cooperatives²², it became clear that also in Hungary the prevalence of distrust in any kind of cooperation due to the communist legacy is a reality. Changing attitudes and overcoming mental barriers are prerequisites for facilitating the emergence of new cooperatives. But how could these be achieved? Interventions from political or other actors situated in the centres of governance will not be effective in changing mental models. This requires decentralised discourses and face-to-face communication at the local level by actors who seriously engage in building social capital. Such processes take time and involve a high cost.

An important problem reported from Hungary is opportunism. Non-compliance of members with the delivery obligation is the main collective action failure in emerging cooperatives. In addition, a strong shadow economy (termed as "black and grey economy") hampers the development of cooperatives (also mentioned in the Polish case study). The tax evasion of farmers in the shadow economy reduces the competitiveness of cooperatives, and the transparency of transactions, which is a precondition for the successful operation of any firm.

²² DélKerTÉSZ: the largest Producer Group in the Hungarian fruit and vegetable sector; Csabai Raktárszövetkezet: a small bottom-up cooperative in the cereal sector; Mórakert: a vertically integrated cooperative in the fruit and vegetable sector which was successful for some years but then went bankrupt.

However, the Hungarian experience also includes successful cases, such as the cooperative Mórakert. Trust in the board of directors, commitment of employees and professional management are considered the main drivers of success and expansion. Unfortunately, this “success story” also had substantial drawbacks: first, entry into the cooperative became too costly for many small farmers. Then, the successful cooperative ran into financial problems due to its rapid growth (too many investments in low-profit activities). Although there was considerable financial support from the authorities, the cooperative eventually went bankrupt.

The internal governance of emerging cooperatives plays a crucial role, in particular, regarding the compliance with strict quality and quantity requirements for the products that are delivered to the cooperative or producer group. To make sure that this precondition for collective action will be met, a careful screening of potential members when members are recruited is necessary.

The Hungarian and Polish cases have in common that qualified, skilled and trustworthy managers, either outsiders or active members of the group, but being professional and having a good education is seen as a core condition for cooperatives to become sustainable. Also, the need to address a pressing economic need through collective action is a significant prerequisite. For example, as shown in the Hungarian case study, farmers appreciate that cooperative members get their payments for their products faster and safer, in other words, reliability and stability represent one of the most important economic requirements. However, cooperatives will only be able to offer these advantages continuously if there are no major financial frictions. For this reason, balancing short-term and long-term liquidity is important, in particular, avoiding the problem of insufficient working capital by means of revolving funds. A well-designed financial structure is a major task of cooperative leaders, but policy makers can facilitate them by providing a stable economic environment, in which efficient credit markets can thrive (long-term policy measures and efficient credit markets). Vertical integration is seen as an important strategy because of the same reason. In summary, an unreliable institutional and behavioural context and expected unstable market and policy conditions play a dominant role against the emergence of new cooperatives in the Hungarian case studies.

8.3.2 The twin cases of Slovakia and Lithuania: rural development following different transition processes

In Czechoslovakia, collective farms were considered particularly important for self-sufficiency and a reliable food supply in the country. This has led to a shared mental model of many inhabitants of Czechoslovakia, which can be interpreted as a socialist variant of agrarian fundamentalism. However, there also were differences between the Czech part and the Slovak part of Czechoslovakia. Slovakia has experienced more land reforms (with braking up of old estates) in the pre-collectivisation period, which means that restitution of land in historical boundaries resulted in a higher degree of fragmentation of land ownership. As a consequence, less former members of collective farms who got their property rights on land back were able and willing to switch to individual farming. This contributed to the preservation of cooperatives, a tendency which was also strongly supported by the agricultural policy of the nationalist Meciar government. In this way, both political beliefs and the legislation on the transformation of cooperatives have influenced the transition process towards a particular outcome: in spite of the challenges they faced during the transition period, transformed production cooperatives have managed to dominate vis-à-vis other types of production and organisation in agriculture. This development and its outcome are in sharp contrast to what happened in Lithuania, where strong anti-Soviet attitudes and a radical liquidation of communist structures occurred (see below).

To enable the development of large cooperative farms in Slovakia, the shares owned by non-members of the cooperatives were not paid to them within the period of seven years as was foreseen by the original transformation laws but were changed into cooperative bonds. The use and trade of these cooperative bonds were subjected to further political and administrative constraints which obviously focussed on improving the sustainability of agricultural production cooperatives. Obviously, the managers of agricultural production cooperatives and their

networks were able to use the political system in improving the sustainability of cooperative farms and discriminate against the interest of outsiders, although the latter had received property rights on the cooperatives assets. Outsiders are not allowed to participate in the general assembly, have no voting rights, and, often, are not accepted as members of the cooperatives.

In addition, cooperatives do usually not follow conventional cooperative principles; for example, the voting rights have usually been changed from “one member one vote” into “voting according to the ownership of shares”. It is an open question to what extent the conflicts caused by this discrimination process have affected the reputation of cooperatives and eroded trust into these cooperative organisations and their leaders. This point could not be sufficiently clarified by the case study, because analysing trust and reciprocity as core elements of social capital is not easy in such situations and requires more in-depth research based on multiple methods.

The development of agricultural production cooperatives in Slovakia (Kabat and Hagedorn, 1997) is quite similar to the development in the Czech Republic (Schlüter, 2001) and East Germany (Beckmann and Hagedorn, 1997) in some important points. Securing the profitability of cooperatives has led to specialisation, simplified organisation and reduction in employment. This implies the problem of aging; in the Slovak agricultural production cooperatives the average age of employees is over 50 years, a group which has only limited labour market opportunities if they had to leave the cooperative.

In spite of the economic pressures on Slovakian cooperatives²³, they still provide some social services in the communities and contribute to rural development. However, these activities are more or less by-products of securing the profitability and sustainability of the farm and also fulfilling legal social policy obligations. For example, they employ many residents of the regions where they are farming and in this way establish a strong relationship between cooperatives and their region. However, this is not the outcome of special regional strategies, but the result of pursuing the individual economic objectives of the firm.

Similarly, cooperatives still provide services to the municipalities but less diverse than before 1990 and mainly for remuneration, not for altruistic reasons. There are minor donations to support cultural and sport activities and schools. However, this can hardly be seen as contributions to the rural society and might also be provided by large, non-cooperative farms. As regards rural development initiatives, for example in rural tourism and environmental protection, agricultural production cooperatives are not contributing as this does not fit in their conservative agricultural strategy.

There is some evidence for a contribution of agricultural cooperatives to social capital and networks, but this was rather weak. Membership in formal associations proved to be limited and trust in personal relationships may have been enhanced by technical assistance offered to other actors, such as small farmers in the region. However, actively building social capital may not be a particular strength of the farms. As regards the use of policy measures, agricultural production cooperatives preferred modernisation and investment policies for their individual farms to marketing and rural development measures. Nevertheless, the positive impact of agricultural production cooperatives on regional employment, in particular on the aging population, and its linkages to the villages and the municipalities, represents positive elements in rural development.

Lithuania

In Lithuania, all Soviet structures such as sovkhoses and kolkhozes were liquidated by the transformation laws and did not emerge again. This development is in contrast to the changes in Bulgaria, where liquidation committees also abandoned the state and collective farms; however, large production cooperatives emerged again for reasons that will be pointed out below. The

²³ Based on the country report and detailed investigations in two cooperatives: Prašice: agricultural cooperative cultivating 4,367 hectares of land; crop production: peas, wheat, barley, oat, maize, rape, sugar beet and forage crops; livestock production: milk and meat, i.e. beef cattle and chicken; Devio Nové Sady: agricultural cooperative cultivating 4,640 hectares of land; crop production: cereals, maize, oilseeds, sugar beet and forage crops; livestock production milk and meat, the latter is decreasing.

radical change in Lithuania, which is similar to the reforms in the two other Baltic countries, can be explained by the historical background, the social attitudes and the political beliefs prevalent in the Baltic societies. As the population of these countries suffered strongly under the communist regime as part of the USSR, in particular during the Stalin era, they strongly desired to return to social and economic structures which had existed before they were occupied by the Soviet Union. Part of this revival was a strong preference of a family farm structure. This was based on restitution policies in land reallocation (from which Russian inhabitants were excluded as restitution occurred only to ethnic Lithuanians).

Establishing a family farm system as intended in the Baltic countries cannot be achieved just by individualising property rights on land and other agricultural assets by means of privatisation. As the agricultural development in many countries has shown, a family farm system can only survive and flourish if the farms are embedded in an environment of other institutions and organisations, such as advisory services, veterinary services, marketing cooperatives, and also a supportive political system that protects small farms against particular risks and takes care of agricultural research and innovation. Obviously, it is this necessity that has induced bottom-up processes in the area of cooperative marketing as shown by the two cases we studied²⁴ that are predominately dealing with milk collection and organic milk certification.

This reveals a sharp contrast to the Slovakian development of post-socialist cooperatives which are large in size and stabilised by top-down policies, whereas the Lithuanian cooperatives are based on self-organisation and intense bottom-up processes. It was local leaders who successfully managed to overcome the communist legacy regarding distrust in any cooperation by establishing “an open line of communication”. In this process, as emphasised in the work by the late Nobel laureate Elinor Ostrom (1995), the rule of face-to-face communication for sustainable establishment of local cooperation is visible: Board members cared and engaged in building trust by paying attention to the concerns regarding cooperation, the management problems and also creative ideas of small farmers. These cooperatives were generating knowledge and contributed to local capacity building by employing a heuristic approach that was appropriate to serve their members’ needs. In addition, not only the members of the cooperative profited from these services and the information provided, but also the whole community. The impact was described as: “Members are proud to belong to a cooperative”.

The services provided by cooperatives and installed by cooperative leaders, in particular by appropriate communication, consisted of packages, for example mastitis treatment, feeding concepts, quality improvement, etc. It appears that the cooperative had a kind of agricultural development function in the local context. Concerning knowledge generation needed for the leaders and members of cooperatives, the problem of small countries, like the Baltic States, is their limited capacity in establishing a training system. The cooperatives contribute to the establishment of networks and to the increase of low incomes as they support small dairy farmers with limited production capacities.

Similar to the situation in other countries, the cooperatives are oriented towards core economic objectives and do not invest in broad initiatives for rural development. This is similar to what was observed in Slovakia. It is clear that the role and the functions of post-Soviet agricultural cooperatives are totally different from the former kolkhozes. Surprisingly, the leaders of cooperatives did not make use of any policy measures for founding the new cooperatives. This result is in contradiction to the evidence gained by the Polish and Hungarian case studies where policy support is considered a necessary condition for the emergence and sustainability of cooperatives. In contrast, the Lithuanian cases studies focussed on the revival of self-help by deliberation, trust building, communication and leaders integrity.

²⁴ Pieno puta: a dairy cooperative collecting milk and other farm products, mainly raw milk, including transportation and storage, collective bargaining, credits for the members; Ekotikslas: a dairy cooperative collecting organic milk and other farm products, including transport and storage, collective bargaining, organic certification.

8.3.3 The twin cases of Bulgaria and East Germany: agricultural production cooperatives

Bulgaria went through a very radical process of transformation after 1990 (Hanisch, 2003). State and collective farms were liquidated and agricultural land was returned to the former owners in historical boundaries. Accordingly, the transition process was not oriented towards a sufficient degree of continuity in the development of agricultural structures as the Hungarian strategy was focussing on. In addition, Bulgaria experienced unstable political conditions reinforced by frequent changes of governments accompanied by equally frequent changes in privatisation and transformation legislation. This contributed to instability in rural areas where poor people and pensioners were living in increasing poverty and sometimes even suffered from hunger in the winter time.

This situation was reinforced by the fact that Bulgaria had several land reforms before collectivisation which implied extreme fragmentation of ownership in land after the restitution process. This resulted in a dual agricultural structure: There are numerous semi-subsistence farms, for example cultivated by pensioners, and large tenant farms, either joint stock, limited liability companies, or agricultural production cooperatives, which rent the farm land often from many individual landowners. Among these, there are many absent landowners and asset owners living outside the villages. They often have no or minor interest in what is happening with their land and assets and in the development of the cooperative.

It is worthwhile noting that this development reveals a major difference between Bulgaria and Lithuania: After liquidation of state and collective farms, agricultural production cooperatives reappeared in Bulgaria whereas in Lithuania they did not play a role in the development of agricultural and cooperative structures.

In Bulgaria, the agricultural production cooperatives, especially those analysed in the case study²⁵, can be considered as leading economic organisers in the region. They rent land from many owners, organise land consolidation and provide services to small farmers, such as machinery, storage, transportation, and access to markets. They engage in crafting local institutions and contribute to a large extent to the local organisation of farm production.

The intensive engagement in rural development by the two agricultural production cooperatives studied in Bulgaria can be explained mainly by two factors. On the one hand, agriculture in Bulgaria played the role of a “model child” in implementing Soviet structures, in particular “agro-industrial complexes”. It was typical for this type of agricultural organisation that they provided diverse rural functions. On the other hand, the two agricultural production cooperatives described in the case study are located in very poor regions where many people rely on employment in the cooperative, cultivating their small plots or even receiving support from the cooperative for securing their livelihoods. For the locals, employment depends on the viability of the agricultural production cooperatives, and many of them would have to migrate if the cooperative would no longer exist, leaving behind the elder generation. Furthermore, municipalities are very weak and not able to maintain basic infrastructure and public services. In this situation, roads, street lightening, kindergartens, community centres, parks, green zones and sports facilities are maintained by cooperatives, although this is not in the immediate profit maximising interest of the firm. The bakery and canteen of the agricultural production cooperatives provide for cheap food. Especially for the poor and aging population, cooperatives serve as a kind of safety net. This is contrasting the results gained in Lithuania, Slovakia and other case study countries where such social activities were strictly excluded.

As regards policies that play a role for the viability of agricultural production cooperatives, direct payments play a dominant role. The same was true for the SAPARD programme in the pre-

²⁵ NIVA-93: agricultural production cooperative cultivating 2,850 ha of land, divided into 200 ha barley, 400 ha sunflower, 300 ha rape, 400 ha corn, 150 ha coriander, 100 ha fennel, 50 ha maize, 130 ha apricots, 20 ha plums, 10 ha peaches, and 10 ha cherry; in addition, keeping 500 bee families, 250 cows and 745 sheep; EDINSTVO: agricultural production cooperative cultivating 3150 ha, divided over 1000 ha wheat, 300 ha barley, 900 ha sunflower, 100 ha lucerne, 300 ha rape, 300 ha corn, 50 ha oats, 50 ha triticale, 150 ha forage maize, and 35 ha melons and water melons; also keeping 745 sheep and 250 cows.

accession period and measures to replace agricultural machinery (EU measure 121 and 123) used after Bulgaria became an EU Member State. The support measures enabled cooperative leaders to modernise the equipment and machinery and, in this way, have not only stabilised the structure of agricultural production cooperatives but also the villages' economy and the safety net for the poor and elderly people. It is important to note that direct payments play a crucial role for the sustainability of the agricultural production cooperatives, which would otherwise be likely to disappear and be replaced by IOFs. These would no longer assume functions outlined above, such as social security, rural development, private and public services and infrastructure maintenance. In other words, particularly in poor and less developed regions of the EU, important impacts of direct payments that go beyond the boundaries of the individual farm are of high political and social relevance. This is an important aspect as regards the presently discussed CAP reforms which include the issue of whether or not (and if yes, how) payments should be subject to a ceiling restriction. Admittedly, part of the direct payments may flow to absentee landowners, but this share should not be overestimated, as they often do not participate in the decisions of the cooperative and, therefore, may be easily excluded from receiving economic surplus.

The most important conclusion from the Bulgarian cases is that agricultural production cooperatives have developed a special type of "ownership" of the villages, in terms of providing infrastructure, services, rural development aid and a safety net for the poor. It may not be an exaggeration to conclude that levels and roles of political governance and economic governance have turned upside down. In other words, political and administrative governance that is usually expected to act at a higher level than the local economy is instead, to a large extent, nested in the firms' governance. This seems to be a survival strategy for the rural society.

East Germany

In contrast to the Bulgarian transformation process in agriculture, the structural and organisational changes of agriculture in East Germany resulted in less friction. Land restitution was limited as only collectivised land was returned to the original owners and nationalised land was not, but it was leased to the existing farms and step by step sold in a long process organised by the German Land Utilisation and Administration Company BVVG (Hagedorn, 1997; Beckmann and Hagedorn, 1997). In addition, the transition of agriculture in East Germany was facilitated by government programmes, such as early retirement schemes, direct payments, and investment and modernisation policies. In addition to these national measures, early access of East Germany to the European Union enabled East German agriculture to profit from favourable support measures, but was also earlier exposed to intense competition.

Transformation of the former collective farms into the present agricultural production cooperatives (preferred over other legal forms of production organisation by roughly half of the collectives) has faced some crucial challenges: securing land tenure in a situation when land has to be rented from many land owners (including members of the cooperatives) requires particular strategies implemented and skills possessed by cooperative management. In particular, in a situation of increasing competition for scarce land that was even reinforced by the bioenergy policy of the German government (mushrooming of biogas plants due to the incentives from the feed-in law for energy), agricultural land becomes scarcer and more expensive. Another characteristic of the development of cooperatives in East Germany is the rapid reduction in the number of employees required, because the farms were modernised and production programmes simplified. To lay off employees (who are often also members) may be risky for the production cooperative as these may withdraw their land and lease it to other farms. An economic strategy towards multi-functional agricultural cooperatives may be considered more sustainable as it avoids such risky decisions, because the level of employment can be maintained and new "profit centres" could be discovered.

The two agricultural cooperatives²⁶ analysed in East Germany have followed different strategies to escape from the “trap” mentioned above. Option 1 is to maintain members’ employment and security of tenure by providing Raiffeisen-warehouse type of services, such as filling stations, repair workshops, storage, etc. Option 2 is producing energy from biogas, photovoltaic cells and wind turbines in order to organise a bioenergy village which includes both the provision of electricity and heating. The difference in strategies compared to the Bulgarian agricultural production cooperatives can easily be seen. Whereas the latter engage in the production of local public goods to secure the survival of the rural society, the first extend their production of private goods to survive as individual firms (or in this case: organisations with some characteristics of a labour-cooperative).

Community services are only offered with remuneration (similar to Slovakia and Lithuania). However, also a considerable and visible donation from one of the agricultural production cooperatives could be observed: together with its employees the cooperative engaged in the restoration of the local castle. The main motivation behind this was to improve the reputation of agriculture in the region and, in this way, build a more favourable social context.

The East German agricultural production cooperatives can be interpreted as examples of institutional and organisation learning for shifting towards a multi-functional cooperative. This is driven by the objective to ensure sustainability by maintaining the level of employment and long-term access to land. A number of activities that could not survive on their own are merged into a joint organisation that economises on transaction costs and benefits from economies of scope. In other words, links to two important local factor markets, labour and land, became part of the cooperatives’ governance concept. As this strategy can contribute to keeping economic activities in rural areas, which were otherwise threatened by the abandonment of agriculture and economic and population decline, the question arises as to whether such strategies of cooperatives should be supported by policies.

8.3.4 Concluding remarks

In an evolutionary perspective, the situation in West and East Europe can be seen as “poles”. In West European cooperatives, adjusting internal governance to the increasing size and internationalisation of cooperatives can serve as an example of the complex type of issues that are at stake. In the New Member States, overcoming the communist legacy, convincing members by building trust, coping with fundamental collective action problems, often in poor regions with vulnerable rural societies, reflect pioneer activities that resemble early stages of the cooperative movement. Any design of EU policies for farmers’ cooperatives or producer groups should take into account such basic differences.

An often prevailing assumption is that the problems of cooperatives are almost identical in Central and Eastern Europe, because they are part of the post-socialist transition. However, reality tells us a different story, as was already concluded in Chapter 3. The issues are diverse and contrasting due to differences in historical backgrounds, pre-collectivisation land reforms, post-collectivisation transformation laws, cooperative traditions and its collective memory, policy streams and the social and cultural context (Hagedorn, 1998). However, all cases have in common that the impact of the communist legacy persists, as lacking trust was identified as a major obstacle to cooperative development in all case study cooperatives.

Thus, an existing economic need for cooperation is certainly a necessary condition for the establishment of a cooperative. Thus, the livelihoods of people or viability of farms often depend on well-functioning cooperatives. However, it is not a sufficient condition. As mentioned, building trust and social capital is one of the main prerequisites for paving the way towards a sustainable cooperative. This cannot be achieved just by fiat. It requires, first of all, a

²⁶ Agrargenossenschaft Hessen e.G.: an agricultural production cooperative cultivating 1,960 ha of land: 1,191 ha wheat, 265 ha rape, 255 ha barley, 131 ha sugar beets and 12 ha corn; Landwirtschaftliches Unternehmen Tangeln e.G.: an agricultural production cooperative having 505 ha, thereof 139 ha grassland; much of the land is leased out, the remaining area is used for 153 cows and 170 head of other cattle.

constructive discourse and communication that takes the problems and ideas of present or potential members into account as well as provides advice and services. What is more, not abstract concepts but practical examples convince would-be members and can induce a snowball effect as shown in the Lithuanian case.

8.4 Human capital

Human capital is the stock of competencies, knowledge, social and personality attributes available with persons to produce economic wealth. It is a very hard to measure but important input in all production processes. It is of course linked to education, but also to creativity and personality. In the previous chapters we have already pointed out the importance of human capital. In Chapter 4 it played indirectly a role in the issues of internal governance, e.g. concerning the professionalization of (supervisory) boards and in the role of professional management. In the analysis on the New Member States in the previous section, the role of human capital became evident, and most of all in the situation of new, emerging cooperatives. This section partly repeats these findings and adds insights from other case studies.

Cooperatives need to invest in human capital development, both of their employees and managers and of their current and future board members. In order to attract and keep expertise and skills, they have to remunerate their employees and managers well, and to offer board members compensation for the time and effort dedicated to meetings and other board activities. Provided that the employees and managers perceive their payment as fair, and compensation for board members are such that they can induce the necessary effort, it may not be necessary to pay (high) bonuses. In case, a contingent payment scheme is used, transparent criteria and evaluations that fit to the core objective (i.e., member benefit) of the cooperative are needed and sufficient information is to be given, to minimise the risk of a break-down of trust.

General technical and entrepreneurial education and training of (future) employees, managers and board members is necessary, but also education and training on how cooperative identity translates into business activities is needed. All parties involved, whether members or managers and staff, need to be aware of the specific characteristics of this form of collective entrepreneurship. Members and managers both need to develop the capacity and the willingness to communicate with each other and jointly develop their business.

Unfortunately, the cooperative business model and cooperative governance have not attracted the attention of agricultural economics and business schools as much as they deserve. Several managers have stressed (also in public, outside this project, even by chairpersons of large cooperatives like FrieslandCampina) the need to train farmer-members so that they acquire the skills necessary to serve on cooperative boards of directors. Training is needed in specific programs, but also member meetings represent essential opportunities for exchanging information, and elaborating on the core identity of the cooperative. Governments can support training and education programs, support the development of curricula and teaching materials concerning the cooperative business model and governance, and stimulate that this be taught in secondary and higher education.

In networks, associations and federations of cooperatives, the internal human capital (of members and employees) of cooperatives can be strengthened. Next to realising economies of scale and market power, these network organisations are important from the perspective of human capital building. Through them, cooperatives can share information, organise mutual learning, offer education and training to their members and personnel, develop joint research and development projects.

Existing (large) cooperatives should consider investing in the maintenance of their human capital, potentially supported by governments, given the positive external effects. For emerging cooperatives the human capital issues are much larger, as the above analysis shows. The question, then, is who should assume the task of initiating new cooperatives and provide leadership, particularly during their first, often difficult, years.

Only trustworthy leaders, who have a strong reputation and adequate education, and are willing to spend years in communication and deliberation processes together with their group

members, will be successful. In addition, sufficient leadership requires professionalism and the ability to perform managerial work efficiently. An adequate salary is required in order to be able to recruit such leaders and managers. Leaders and managers with such capacities will then be able to cope with opportunism of members, such as non-compliance with delivery obligations, thus preventing collective action failure. Such leaders probably represent the scarcest factor for a new cooperative movement in post-communist societies - and elsewhere.

Although many scholars emphasise that cooperatives, being based on self-organisation, should develop independently from external hierarchies, our findings on the New Member States reveal that there is a strong role for a facilitating state. The Lithuanian case study surprisingly showed that the cooperative leaders did not use policy measures but built the group by strengthening the cooperative's own forces – but this seems to be an exceptional case in which the transition period was characterised by an extremely strong desire to break down USSR structures and adopt family farm structures. In the other New Member States cooperatives used and were sometimes even dependent on government policies to establish cooperatives, but most of these policies had more to do with funding (investment aid, direct payments, energy-subsidies by the feed-in tariff etc.) than with strengthening human capital.

Nevertheless the knowledge and skills and the role of advisory services and training activities were often mentioned in the interviews as being important. Building a knowledge system for the community involved in agricultural cooperation is a demanding task. Assistance from and exchange with the cooperative systems in other EU-countries could certainly help, provided that such arrangements would be carefully chosen – we found a nice example of a “tutelage” (or tutorship) between a French and Romanian cooperative (not for business reasons but as a support activity).

It is important to be aware that this cannot be achieved only by involving academic or government experts. The analysis of transnational cooperatives in Chapter 7 shows that they play a role in providing technical know-how in other (New) Member States, but that seen the interest of their members and managers, it is not to be expected that they will transplant the cooperative model automatically.

An appropriate policy should also engage practitioners from cooperatives and producer groups and different sectors of agriculture and horticulture. This requires well-organised processes of knowledge generation and communication. In other words, just occasional visits and courses will not be sufficient. Instead, well-designed partnerships maybe an effective - although demanding - setting where experts and practitioners engage in long-term exchange and processes of mutual learning and carefully crafting elements of the educational and advisory system. Governments can provide structural support to these networks and projects for human capital development. The targets of such programs should not only be cooperative (board) members but farmers in large. Knowledge within credit, education, extension and policy making institutions is important, too. The importance of awareness rising, creating a culture of cooperation, and informing society about the benefits of cooperatives (as forms of organised cooperation) cannot be overemphasised.

A difference between Canada and Belgium, two countries that are quite active in implementing support measures for cooperatives, is the level of coordination among policy measures in support of agricultural cooperatives. The importance of a coherent and integrated policy framework cannot be overemphasised. Especially in federated countries the various policy levels need to communicate and develop coherent policy measures for cooperative development in all economic sectors. The Cooperative Development Initiative in Canada was intended to integrate information concerning the specific cooperative business model and measures to support its development. It has led to an enhanced accessibility of measures for cooperatives and their associations, to an improved collaboration among governments, practitioners, cooperative experts and associations of cooperatives at all levels. It has also led to the formation of new cooperatives, also in regions with little tradition of cooperative entrepreneurship. We come back to these policy issues in the next chapter.

9 Institutional environment: legal aspects and policy support measures

9.1 Introduction

An important part of the institutional environment, in addition to the social and cultural characteristics discussed in the previous chapter, is formed by the legal and policy aspects. They merit an extensive discussion, also as policy makers are one of the main audiences of this study. Some legal and policy support issues have already been discussed in previous chapters. In Chapter 5 legal aspects in relation to internal governance were already discussed, a topic we take up again in the next section where we discuss the (basic) legal regulation that governs cooperatives. This is followed in section 9.4 with issues related to (international) mergers, competition and – unrelated to that, tax issues.

These two sections deal with the legal issues that often are not specific to agricultural cooperatives and certainly not the traditional domain of policies in agriculture, food or rural development. Section 9.6 adds those types of policy support measures to the analysis. Before doing that we devote section 9.5 to the relationship between cooperatives and rural development.

9.2 Legal regulations for cooperatives

Although there is no evidence that Member States actively promote the organisation of agricultural producers into cooperatives nor mandate that they should use the cooperative as the legal business form, the cooperative is commonly used in the EU and appears to be the “natural” legal form for agricultural producers to organise their joint business activities. The cooperative statute is not commonly used in Bulgaria, Estonia, Latvia, Poland, Romania, Slovakia and Slovenia, where the limited liability company is the dominant legal entity in which agricultural producers organised themselves. In Portugal, the division is 50/50. Despite the low numbers of cooperatives in several countries, the cost of setting-up as well as maintaining a cooperative does not seem to hamper the formation of cooperatives.

In terms of internal governance, the data did not identify significant constraints to efficient decision making imposed by problematic legislation. On the contrary, legal frameworks are considered flexible enough to allow the development of proper internal governance structures. In large cooperatives, in particular internationally operating cooperatives with diversified activities, there is some concern about the perceived loss of effective control by members.

Only in four Member States members seem to feel an accountability gap. The accountability of the board of directors to members in Greece, Portugal, Spain and the UK is seen as more problematic due to the lack of legal mandates to form a supervisory board or an similar institution – although members could use the bylaws for initiating such a board.

The efficiency of cooperatives could be improved by hiring professional managers, while the monitoring of the board of directors could be enhanced by installing a supervisory board.²⁷ In Bulgaria, Cyprus, the Czech Republic, Greece, Malta, Portugal, and Slovakia, the members of the board of directors can only be members of the cooperative. Sixteen Member States provided the possibility of having non-members elected on the board. In seven Member States, members of the supervisory board need to be members of the cooperative. However, it does not necessarily mean that there is an accountability gap. If cooperatives are small and operating only in the region, leaving members themselves in the position to actively monitor the management board may not pose any problem. On the other hand, in several countries the lack of leadership and relevant competences is seen as problematic for the development of cooperatives.

²⁷ A recent law made supervisory boards mandatory in Greek agricultural cooperative.

Most Member States allow cooperatives to restrict entrance of new members through provisions in their bylaws. The “defined membership” policy is usually intended to protect processing cooperatives from having to handle raw material well in excess of their processing capacity or the quantities they have contracted for with retailers. In countries such as Denmark, France, Hungary, and Ireland, however, the “open membership” principle is legally enforced. In Denmark, for example, a cooperative holding a dominant market position may be legally forced to accept new members.

Directly related to the question of open membership is the question of whether voting rights are allocated according to the principle of “one member, one vote”, or whether the cooperative is free to use voting rights proportional to the volume of economic transactions of the individual member. In ten Member States, the principle of “one member, one vote” was the mandatory rule. In eleven Member States, cooperatives were allowed to apply proportional voting, however with an upper limit on the number of votes, while a minority of Member States allowed proportional voting without any upper limits set by law.

Most Member States do not provide cooperatives with effective legal means to control the volume of produce supplied by members. These Member States adhere to the principle of voluntary membership by giving members unrestricted freedom to exit the cooperative (Cyprus, the Czech Republic, Denmark, France, Italy, Latvia, Lithuania and the United Kingdom). In these countries, the free rider problem poses significant challenges to many cooperatives. In the other Member States, cooperatives were allowed to introduce restrictions, showing a large variety of modes over time. Two important findings are: 1) in all members states the restrictions on exit were viewed as reasonable and fair, indicating that setting restrictions on exit is not considered problematic; and 2) the existence of restrictions on exit did not preclude potential members from joining a cooperative.

No evidence was found that national cooperative statutes contain legal restrictions on the acceptance of members from other Member States or on the exercise of their membership rights. Taking into account the established case law of the ECJ on the freedom of movement, cooperatives encounter no restrictions in setting-up subsidiaries in other Member States. The SCE Statute has not been used until now by agricultural producers to form a transnational or international cooperative. Questionable is whether potential members from another Member State can be barred from becoming members, if this represents their sole reliable option. The taxation of members from other Member States has not led to significant problems so far, with the exception of two cases in Sweden/Denmark and France/Germany.

With regard to the question whether cooperatives are restricted by law to organise the cooperative as a group, with the cooperative as the parent company, Member States do not impose any restrictions on cooperatives. However, there might be severe tax consequences (see next section).

As processing and marketing cooperatives are capital intensive, and finance can be problematic (see Chapter 5) the question is whether cooperatives are legally able to distribute net proceeds taking into account the proportion of capital paid in by members. Our legal analysis shows that cooperative statutes do not restrict members to create tailor-made solutions in their bylaws. It is common practice that the distribution of surplus to members as well as their obligations to participate in self-financing techniques of the cooperative is executed on the basis of the principle of proportionality, according to the volume of transactions of an individual member with the cooperative. In this respect, it is worth mentioning that 22 Member States were reported to have flexible legal rules on the distribution of surplus to cooperative members. However, retaining surplus and accumulating reserves may trigger a loss of the favourable tax treatment.

The virtual absence of raising equity from outside investors is not caused by the lack of an adequate legal structure. Only seven Member States (Belgium, Bulgaria, Cyprus, Estonia, Portugal, Romania and Slovakia) did not allow outside investors to participate in the equity capital of the cooperative. Accordingly, in these Member States voting rights could not be allocated to non-patron members. However, it remains questionable whether in these Member States there is a genuine demand for this legal facility. The other Member States allowed or,

more accurately, did not forbid outside investors to participate in raising equity. However, in a substantial number of these Member States this facility was not aligned with the allocation of voting rights to outside investors (Finland, Greece, Hungary, Latvia, Lithuania, Malta, Poland, Slovenia, Sweden and the UK). But even in Member States with both facilities, raising equity from outside investors is still in an embryonic stage. Hence the conclusion that the legal structure of the cooperative is not a dissuasive factor for obtaining equity capital from outside investors.

Overall we conclude that legal structures are not a major hurdle for farmers to cooperate effectively and organise their business according to their strategy. In some countries like Denmark and the Netherlands the legal structure is extremely flexible and has provided cooperatives with room for experimentation and expansion. In other countries legal structures are more restrictive, but this seems often not to be a problem (as cooperatives are smaller or less capital intensive), as restrictions may be overcome through other means. However, this also means that the legal structures do not provide much guidance for good practice, which in some Member States might be beneficial. More legislation is not needed, better legislation is possible but it is not the ultimate solution in promoting cooperatives.

9.3 Mergers, competition and tax issues

With regard to domestic merger legislation, all Member States do have legal provisions for cooperatives to merge with other cooperatives. In Bulgaria, Ireland, Luxembourg, Poland, Portugal, Romania and Slovakia, cooperatives are not permitted to merge with non-cooperative firms. On the other side, Austria, Belgium, Germany, Hungary, Greece, Lithuania and Spain provide a highly flexible set of rules on domestic mergers. The largest group of Member States have rules on domestic mergers between cooperatives and with IOFs, although with several highly path-dependent restrictions. In Spain there are some impediments for cooperatives from different autonomous regions to merge with cooperatives based in another region. In general, the efficiency of mergers is not negatively affected by rules of employee involvement or taxation vis-à-vis IOFs.

The provisions for cross-border mergers between cooperatives remain fragmented. The SCE Regulation provides the necessary facilities for cross-border mergers, but the SCE is not used in practice by agricultural cooperatives. Transnational and international cooperatives maintain their internal governance structure based on national cooperative laws; they (and their legal advisors) have experience with these regulations, including jurisprudential history. Switching to the SCE seems to be too costly and risky.

The 10th Directive on cross-border legal mergers of IOFs did not have a significant harmonising effect on the ability of cooperatives to engage in a cross-border merger. Although the right to participate in a cross-border merge between cooperatives from different Member States can be based on the ECJ case law, notably the *Sevic System AG*-case, this possibility lacks legal certainty.²⁸

The SCE Statute could be useful for the development of cooperatives in developing regions and the New Member States. The European SCE Statute provides a state of the art of internal governance, but it is a top-down and has a “one size, fits all” approach that in its current form is too complex to apply for small start-up cooperatives; at best, the current SCE Statute could function as a model act for national legislation that will be needed in the coming decades given the evolution of the cooperative law, the differences in cooperative business cultures and the differences in challenges facing cooperatives in each of the Member States.

²⁸ Legal certainty is a principle in national and international law which holds that the law must provide those subject to it with the ability to regulate their conduct.

Competition

Effective competition is an integral part of agricultural policy objectives and competition rules are part of the regulatory framework of the agricultural sector. When assessing competition rules applicable in the agricultural sector, the legal framework consists of general EU competition provisions (i.e., Articles 101 to 106 TFEU²⁹ and all implementation provisions), EU competition rules specific to the agricultural sector, and national competition legislation.

Article 42 TFEU Section 1 establishes that competition rules apply to production of and trade in agricultural products only to the extent determined by the European Parliament and the Council, taking into account the objectives of Article 39 TFEU. In accordance with article 42 TFEU, the Council has adopted two regulations currently in force, which establish the relation between the rules of competition and the CAP, i.e., Regulation (EC) 1184/2006 applying certain rules of competition to the production of and trade in agricultural products and Regulation (EC) 1234/2007 establishing a common organisation of agricultural markets and on specific provisions for certain agricultural products.

The EU competition rules do not apply unless the agreement or practice has effect on trade between the Member States. Cooperatives that only trade regionally or nationally, do not have an effect on intra-EU trade. In such a situation, national competition rules apply. All Member States currently have national competition legislation that mirrors the rules set out in Articles 101 and 102 TFEU.

In EU competition law cooperatives are assessed, like any other company, on the actual effect of their behaviour in the relevant markets. When assessing the application of Article 101(1) of the TFEU to cooperatives, the Court of Justice has clearly recognised in several occasions the pro-competitive effects stemming from cooperatives and established that the prohibition principle of Article 101(1) does not apply to certain provisions of cooperative agreements, for instance where they are indispensable in order to create countervailing power.³⁰

A joint production agreement in the agricultural sector is another example of cooperation agreement that is favourably assessed under the EU competition rules. Under such an agreement farmers group together, as a cooperative or under another name or statute, their complementary productions at an upstream level with the aim of producing agricultural products (wine, cheese, flour, fruit preserves etc.) at a subsequent processing stage. A joint production agreement is unlikely to restrict competition if the parties to the agreement do not have market power in the market on which a restriction of competition is assessed. In fact, joint production agreements benefit from the presumption under EU competition rules that if they are concluded between parties with a combined market share not exceeding 20% in the relevant market(s) they do not restrict competition.³¹ Above this threshold, a joint production agreement may be allowed if it is possible to demonstrate by an individual assessment that the efficiencies created by the agreement outweigh any competition restrictions.

An often discussed issue for the application of competition rules to cooperatives is the relative strength of the contractual relationship between members and cooperative. A cooperative can enhance its competitiveness by having strong contractual ties with its members. These contracts are meant to clarify the quality requirements that farmers have to comply with (and to explicate the accompanying monitoring and control mechanisms), as well as to restrain farmers from short term exit (as that would jeopardize the efficiency and thus competitiveness of the cooperative firm). In order to avoid excessive market power by a cooperative the Court of Justice's case law³² requires to analyse the members' possibilities to exit or withdraw from the

²⁹ TFEU = Treaty on the Functioning of the European Union

³⁰ Case C-399/93, *Oude Luttikhuis*, p. 12. Also Case C-250/92, *DLG* p. 32: In a market where product prices vary according to the volume of orders, the activities of cooperative purchasing associations may, depending on the size of their membership, constitute a significant counterweight to the contractual power of large producers and make way for more effective competition.

³¹ Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements. Text with EEA relevance OJ C 11, 14.1.2011, p. 169.

³² C-399/93, *Oude Luttikhuis*, p. 13-19

cooperative (so that they can operate autonomously or potentially join another competing cooperative) and their freedom to supply third parties other than the cooperative itself.

The overriding principle, however, has been that restrictions upon member exit are not perceived as infringing on competition rules when they are deemed necessary for the cooperative to function efficiently from an economic point of view. Whether the restrictions are necessary has to be established on a case-to-case basis. In this respect, several determinants have been established in case law: market share, the number of other market competitors, whether other market competitors use the same restrictions, whether members are allowed to contract with other market competitors or exclusively with the cooperative, whether an accumulation of restrictions has the power to prevent members from contracting with other market competitors.

In a specific case, EU competition rules might not apply to a particular cooperative recognised according to article 122 of sCMO Regulation where exceptions stated in article 176 of sCMO Regulation are met. The potential application of these exceptions to a PO or farmers' cooperation agreement only becomes relevant when the agreement at issue may fall under the scope of application of Article 101(1) (that is, when it may actually or potentially affect trade between Member States). Article 176 of the sCMO Regulation states, essentially, that the Article 101(1) TFEU shall not apply to agreements of farmers and their associations belonging to a single Member State if the agreements concern the production or sale of agricultural products *provided that* such agreements do not fix prices, do not exclude competition and do not jeopardise the objectives of Article 39 TFEU. If these conditions are not fulfilled, the agreements can still be authorised under article 101(3) TFEU provided the conditions of that article are fulfilled.

Clearly defining the objectives pursued by agricultural cooperatives seems to be a prerequisite for the efficient promotion and development of these unique institutional arrangements. Otherwise there is a risk of conflict between national legislation and CAP provisions. Also specific rules on forms of cooperation that could by their nature or structure possibly affect trade between Member States (for example, national price arrangements, export taxes or funds, etc.) may be necessary.

Most importantly, national provisions on cooperatives and the EU competition rules must be coordinated. There are numerous cases, where cooperatives may have an effect on trade between Member States. For example a market organisation concerning pricing arrangements of exports or imports or joint purchases from other Member States is by nature international. A nationwide market organisation will always be considered to influence the terms of trade between Member States. Further, transnational cooperatives will most likely always have a significant effect on trade between Member States.

To prevent legal uncertainty due to different legislation in different Member States, it would be helpful to assess which forms of cooperation are as such compatible with national competition laws. If the aim is to promote POs in the agricultural sector, it could be recommended to assess whether general rules are enough or whether specific provisions are required on the national level, from the point of view of different types of cooperatives and different product markets. The scope of activities of the PO, the effects on competition and the content of the activities in relation to the objectives of article 39 TFEU must all be taken into account in this assessment.³³

There is a difference between the EU Member States and several other OECD countries as to the application of competition law. Particularly in the USA the Capper-Volstead Act provides for broad anti-trust exemption for agricultural cooperatives on the ground that they strengthen competition in agricultural sectors where farmers have low bargaining power vis-à-vis their processing and trading customers. However, the conditions under which the Capper-Volstead

³³ In several of our case studies, notably in the F&V sector, representatives of the cooperatives voiced complaints about the behaviour of the National Competition Authorities, both about the grimness with which they scrutinize collaboration among cooperatives and about the legal uncertainty that these authorities maintain by not being clear about their definition of the relevant market.

Act applies are rather restrictive. For instance, the exemption only applies under the condition that the cooperative does not have non-member users and does not pay members in any way for capital invested irrespective whether this is done according to the volume of patronage.

Several of our case studies, especially but not only those in the New Member States, reveal that cooperatives improve market efficiency in several ways: they challenge monopsonistic markets and powerful international conglomerates in Poland and Hungary, deal with difficult access to the dairy market (including organic) and milk processing in Lithuania, provide market access to smallholders in Slovakia and Bulgaria, enter the farm and energy supply markets in East Germany, establish links to the land and labour markets both in Bulgaria and East Germany, and so on. In such cases the contribution of cooperatives towards efficiently operating markets seems to be much more significant than any risk of upward pricing pressure, but of course this has to be evaluated on a case by case basis.

Tax issues

The way cooperatives are treated by the tax authorities in the majority of Member States, seems to facilitate their growth. Cooperatives are treated as an extension of members' farms. Consequently, surpluses (money earned from selling members' products) return to members in cash or held in individual accounts by the cooperative and are taxed only at the farm level (single taxation principle). Profits, that is, money earned from selling non-members' products, are taxed at the cooperative level and, if distributed to the member, also at the farm level. In some countries, cooperatives' profits are not taxed at all at the level of the cooperative, even in case they are kept in special reserves (e.g., for investments in R&D or education). Such provisions are particularly helpful for new and growing cooperatives but not of much relevance for large cooperatives that conduct significant transactions with non-members. In some countries, the taxation of cooperatives is under discussion (e.g., in Spain, where the focus is on clarifying the types of cooperative capital).

Finally, it should be realised that in some cases small farmers are sometimes not willing to join a cooperative as they prefer trading in informal markets with opportunities to evade paying value added tax or income tax. This behaviour has mostly disappeared in other countries where scale and professionalization of farming has increased and where farmers and cooperatives participate in tightly coordinated supply chains which include tracking and tracing systems for food safety, liability and certification reasons.

9.4 Cooperatives and rural development

Before moving from the issues of mergers and competition in the food chain to policy measures in support of cooperatives, this section examines the role of cooperatives in rural development.

The links between cooperatives and rural development are manifold. Cooperatives are more likely to be set up in remote areas facing market access challenges (e.g., long distance transport to the market) and information asymmetry (dependence on traders for price information). Markets can and do fail in such regions. Cooperatives support income and employment in areas where rural development is a policy issue.

Cooperatives in more remote areas are often important employers and also contribute in other ways to the economic and social development of a region. In many cases the activities of these cooperatives go hand in hand with support for pursuing public objectives such as the development of human capital and environmental protection. Cooperatives promote and lobby for public programs, including subsidies, that favour the region. Cooperatives can also have a positive effect on prices that other farmers, who deliver to IOFs, receive (the so-called competitive yardstick effect, see Chapter 6). Further, in sharp contrast to their IOF counterparts, agricultural cooperatives are tied to a particular region because the farmers who own, control and are benefitting from the cooperative are also tied to the region through ownership of land. Thus, in case profit margins decrease cooperatives would keep servicing their member-owners and the local community while an IOF would seek better business opportunities elsewhere.

In some cases cooperatives build their business strategy even on regional characteristics

and social processes (resulting in, e.g., regional or fair trade-type of products and services). PDO-PDG-type of products and links with incoming tourism can be part of such a strategy. However, in the end, all cooperatives are business oriented: there has to be an income from the market (but sometimes supplemented by subsidies).

Cooperatives are economic organisations, and activities that do not fit in their business models are not taken up or are discontinued, sooner or later. Like IOFs inside and outside agriculture, many cooperatives perform activities that are inspired by their corporate social responsibility policy. They help the communities in which they are located and make donations to good causes in money or in kind (e.g., time of employees). Of course these activities are not without some self-interest, as they support marketing, public relations, and employee satisfaction strategies.

It is also clear that in some regions the cooperative is not only an important element in the life of the farming and rural community, but also an important social “place” to meet, to learn and socialize. However it should not be expected that cooperatives pursue rural development as their primary objective. Also in the New Member States the cooperative is now, in this respect, business oriented and totally different from the situation under socialist rule. We came across one important exception: in some regions in Bulgaria (and perhaps also in Romania), the political and administrative governance is so weak that, to a large extent, the local communities depend on the cooperative for many social functions.

9.5 Support of farmers’ cooperatives with policy measures

Experience has shown that government policies can impede or enhance independent cooperative development (Hoyt, 1989). For encouraging the development of cooperatives, public policy has multiple points of entry where it can have a significant effect. In support of cooperative development, policy could opt for indirect measures, for instance through provisions in business and organisation law that make it relative easy to establish a cooperative. Also, more direct measures can be taken, for instance in the form of subsidies or grants to producer organisations. By identifying policy measures that affect cooperatives and their development, we aim to provide more insights into policy measures that might contribute to creating a conducive policy environment for the development of cooperatives and producer organisations.

As described in section 2.2, we gathered data on all policy measures that experts thought to have an impact on the development of cooperatives at the Member State and the EU level, and had them assessed by national experts. In some cases these experts worked with interviewees on this assessment. In total, 318 European, national, and regional policy measures have been identified. Table 9.1 breaks this down into several categories of policy measures (see section 2.2. for explanations) and gives details for each of our building blocks. Cooperative legislation, competition rules, inducements (money transfers) and financial incentives were among those reported most often.

When governments want to influence the performance of cooperatives, measures that directly target the position of the cooperative in the food chain are the most cited among our building blocks. Financial or other incentives (including tax), inducements, and cooperative legislation are the most relevant types of policy measures. Internal governance is seen much less as target for intervention (54 measures), and, of course, cooperative legislation is then the most used policy type. Capacity building and technical assistance are much less used as policy measures to improve internal governance, and when capacity building is used, directly improving the position in the food chain (e.g., with marketing knowledge) is a more important goal. About two thirds of the policies try to correct market and regulatory failures and only a small number try to obtain only equity and social goals.

There exist large differences in the policy measures between Member States. Although this might be due to differences in what is seen as a relevant policy measure in the Member States. With 64 policies, Belgium has the longest list of cooperative-related policies. Other countries with considerable numbers of policies are Bulgaria, Greece, Hungary, Latvia, Poland, Romania,

and Spain (all around 20 policies). The large number in Belgium is not only explained by its long cooperative history, but especially also by the federal structure of the country: the different regions (Flanders and Wallonia) also generated a considerable number of policies independent from each other (which means that an individual cooperative or farmer working only in one of the regions is targeted by less policies). Also Spain is characterised by regional policies. Countries with few policies aiming at cooperatives are Luxembourg (1 policy), Estonia (2), and Austria (3). In the case of Estonia this is probably linked to its free market orientation and a consequence of the country's lack of cooperatives, in total, just ten agricultural cooperatives operate in Estonia. For Luxembourg, the low number of policies is explained by deliberate choices of the government. Until 1980, a number of policies specifically targeted cooperatives. Then it was decided however to replace these cooperative-specific policies by measures for all agricultural enterprises (which do not affect the relative position of cooperatives).

We investigated potential links between the support measures for farmers' cooperatives and the performance of cooperatives in terms of market share. This did not lead to very clear insights, perhaps because we correlate current performance with current policies, where market share might be much more influenced by past policies (and we do not control for other factors like social variables).

Table 9.1: Policy measure types per building block (share of policy measure per type in % and total number)

	Policy Measure Type									
	Mandate	Inducement	Capacity building	System change	Other	Cooperative legislation	Competition law	Financial and other incentives	Technical assistance	Total number (=100 %)
General	18 %	32 %	2 %	5 %	0	5 %	36 %	2 %	0	44
Position in food chain	8 %	20 %	5 %	1 %	2 %	15 %	14 %	33 %	3 %	133
Internal governance	22 %	13 %	7 %	6 %	0	44 %	2 %	6 %	0	54
Institutional environment	11 %	18 %	10 %	11 %	2 %	13 %	21 %	10 %	2 %	87
Total number	40	63	20	16	5	57	54	57	6	318

Note: The shares of the most dominant policy types for a building block are presented in bold

The countries with a high market share of cooperatives (Austria, Denmark, Ireland, The Netherlands, Malta, and Sweden) show quite different results concerning the policy environment. For some of these countries (Austria, Malta) the policy measures are seen as quite supporting, for others (Ireland, to a certain extent Sweden that has a cooperative climate, but where foreign transnationals are dominating) as neutral or slightly supporting. The types and targets of support measures do not differ clearly from the EU average. All the countries with strong cooperatives, except the Netherlands, are among the countries with just a few policies targeting cooperatives. This suggests an inverse relationship: when strong cooperatives are formed, less governmental support is offered or needed. There are also countries where a small number of policies are correlated with a small market share, like Estonia and the Czech Republic. This could be explained from a political economy perspective: if cooperatives hardly exist, there is probably a limited lobby for support, especially in a case where economic liberalism dominates policy thinking – as has been argued above in the case of Estonia.

The countries with a relatively low market share for cooperatives (the three Baltics, Slovakia, Hungary,) show quite different policy environments. Some have many policies (like Hungary) others only a few (e.g. Estonia). In some cases they are classified as quite supportive, in others as neutral.

The overall results of this analysis for the EU have a striking similarity with the conclusions of the investigation on policy measures in other OECD countries, notably Australia, Canada, New Zealand, Norway, Switzerland and the USA. That investigation, using the same methods of

classifying and scoring policy measures, found that the absence of policies that support cooperatives can have positive as well as negative effects. A flexible cooperative law is helpful to develop internal governance. In addition, tax systems seem to be important as well as competition rules. The latter do not have to favour cooperatives, but they can be problematic if they do not take into account the specific nature of cooperatives. Also in other OECD countries experts had mixed opinions on technical support for cooperatives by the government. A detailed comparison between Canada and Belgium (both federated countries with a large repertoire of support measures for cooperatives) showed that the main difference between the two countries is – until recently – the high level of coordination within Canada among the different policy measures by its Cooperative Development Initiative (see section 8.4).

We conclude this analysis of policy measures with some remarks on individual policies. The case studies in the former socialist countries made clear that cooperatives also benefit from the direct payments of the agricultural policy (Bulgaria) and the national energy policy (eastern part of Germany, referring particularly to agricultural production cooperatives). In Poland and Hungary, policy support for emerging cooperatives is highly appreciated, and a strong pledge is made for extending the measures by including investment support and balancing budgets for achieving a longer term financial strategy, thus, enabling vertical integration. One of the key learning points is that it takes time to bring cooperatives to self-sustaining organisations. On the other hand there is the Greek experience (see Chapter 3) of cooperatives becoming too politicised.

A topic that might receive more attention in impact assessments of the CAP, is the effect of changes in the CAP on cooperatives. A case study on sheep suggests that the common agricultural policy reforms can have very different effects on successful cooperatives. In Scotland (UK) the reform is criticised as it has negative impacts on hill farming (with reforestation as a result) and takes away volume and specialisation effects that are critical in the business model of the cooperative auction. In Extremadura (Spain) the same reform leads to more professionalism in sheep breeding, of key importance for the second-tier feedlot and marketing cooperative. There the reform is seen as positive. In the wine industry also positive effects of the CAP reform on cooperatives have been reported, and in sugar the reform has led to the adjustment of strategies adopted by the leading cooperatives (see Chapter 6).

10 Main conclusions and implications for countervailing power

This chapter presents the main conclusions of the study. Also, it summarises derived implications for facilitating and supporting farmers to organise themselves in cooperatives as a means of improving their market position and thus generate a solid market income, particularly given the observed imbalances in bargaining power between the contracting parties along the food supply chain.

10.1 Main conclusions

Producer organisations, primarily in the form of agricultural cooperatives, are crucially important business organisations for European farmers. Most farmers are members of at least one cooperative, and even non-members trade with them or benefit from the presence of cooperatives in particular markets. However, this fact is not much prevalent in agricultural statistics and research, and only partly addressed in agricultural policy, with the exception of the CMO in fruit and vegetables and the reform of the dairy policy.

Cooperatives can be considered as a substitute for the market but they are not fully vertically integrated firms that replace a market where transaction costs are too high. Cooperatives are typically hybrid governance structures (Menard, 2007). This means that cooperatives combine elements of markets (like the price that continues to play its motivational role in the transaction between farmer and cooperative) and hierarchy (like the ownership relationship between members and the cooperative firm).

A cooperative is a user-owned, user-controlled and user-benefitted organisation. However, joint ownership and joint control of farmers over firms downstream in the food chain is not limited to cooperatives. Other companies with other legal forms may also be owned and controlled by farmers, often through producer organisations or farmer unions. However, in these cases there is not direct user control. Where producer organisations and farmer unions are the shareholders of an IOF, the latter works in the interest of all the farmers who are members of the owning organisation. The membership includes farmers supplying to the jointly-owned firm, but may also include many other farmers who do not transact with that firm. A farmer-owned IOF is more likely to pursue the interests of a whole farming community than the interests of a narrowly defined group of users.

Whether farmers are better off being members of a cooperative or being contract partners of an IOF is not ideologically or politically determined but depends on the particular characteristics of the product, the farm and the market. Also, farmers have differential preferences as to cooperative membership. The benefits of cooperatives, in terms of improved farmer bargaining position in the food chain, vary with time, place, technology, scale of farming, and human and social capital available.

Cooperatives have clear functions....

Historically, cooperatives are not replacing markets, but help to create them or make their outcomes more efficient. Primary and federated (or second-tier) cooperatives solve efficiency problems caused by the constraints small-volume farmers face in benefitting from economies of scale and in bargaining. Cooperatives help farmers to access markets and to obtain a better bargaining position. These functions are especially important in remote areas where farmers are faced with thin markets, which are often characterized by asymmetric information between seller and buyer and where farmers depend on only a few (large) traders or processing companies. The European sheep sector is an illustration of this: important sheep cooperatives are found in traditionally remote but specialised production areas like Scotland and Extremadura (Spain); in most other regions more buyers are active or low specialized farmers sell to the local butcher or the informal economy. The strong position of cooperatives in the dairy and fruit & vegetables industries can be explained by the high transaction costs that result from the perishability of the product. Once a product is harvested, it has to be processed and/or

sold as soon as possible, which makes the farmer very dependent on the buyer. Farmers have set up (auction) cooperatives in order to reduce the risk that accompanies this dependency.

Most large cooperatives have been formed in past decades in order to address one or more of the abovementioned market failures. As the years went by, however, and the competitive yardstick effect of cooperatives resulted in an efficient market, subsequent generations of farmers have no personal experience of the industry in times of hardship caused by market failures. Therefore, the motives of younger farmers to participate in agricultural cooperatives may be quite different from those of their (grand)parents. However, for cooperatives in the New Member States, the reasons for farmers to set up cooperatives may not be so different from the ones that prevailed fifty or hundred years ago for the members of the now fully established cooperatives.

... and are found in all Member States and sectors

All European Member States have a cooperative tradition that goes back to the Rochdale and Raiffeisen innovations in the 19th century. However, there are important differences between Member States in history, operation and market share of cooperatives. Historically, in some countries the cooperatives are directly linked to large transitions at the end of the 19th century (Denmark, the Netherlands), or a movement for independence (Finland), while others have seen periods where cooperatives were politically not appreciated (Portugal and Spain), or where cooperatives were not based anymore on self-organisation principles but were a socialist planning tool (New Member States). In some countries the labour movement has played a key role in cooperative development, in others it was the Catholic Church. Such diverse evolutionary paths imply that the label "cooperative" has different connotations in different regions.

Cooperative enterprises are sometimes stereotyped as successful, internationally-oriented businesses in northwest Europe, traditional and socially oriented, struggling with internal governance in the Mediterranean Member States, and problematic in New Member States due to their socialist heritage. Although there is a grain of salt in these stereotypes, the reality facing policy makers is more complex and the description is outright wrong for many cooperatives - especially for many successful cooperatives in the South and East of Europe.

Some sectors are more cooperative than others. This is mainly due to the characteristics of the product and the production process. As explained above, in the dairy and fruit & vegetables sectors cooperatives have an important market share. In sectors like cattle, pigs and sheep the products are more often sold by farmers, often under contracts, to traders or IOF slaughterhouses, but in some countries (hybrid) cooperatives have important market shares in these sectors.

Internal governance is diverse

Depending on the options provided by the legal framework in each country, farmer-members may choose among many different models of governance the one that best fits their needs. These models differ among others in the use of supervisory boards, membership councils (in addition to the General Assembly), separation of association and firm, use of professional management, participation of outside experts on boards, non-member trade and voting in proportion to the value of transactions. However, among the 500 well-known cooperatives in the eight sectors we surveyed, most are relatively small and regionally based cooperatives with a classic internal governance structure. Cooperatives do not easily change their internal governance as that brings quite some uncertainty for members and cooperative leaders. Also the influence of legal and fiscal advisors may lead to conservative choices.

Innovation in internal governance benefits from a flexible cooperative law, so that members can use the bylaws to adapt the governance to their needs. That implies that the law does not give much guidance, e.g. on internal control. In some cases checks and balances in the internal governance can be improved, e.g. by installing supervisory boards and the enhancement of professionalism of (supervisory) board members.

Internal governance is directly related to ownership structure. Some of the (innovative) ownership structures are hybrids, with different organisational arrangements like a cooperative

association owning an IOF-like business, producer organisations that jointly own a cooperative, firms owned by farmers' organisations or cooperatives being majority owner of an IOF that is also listed at the stock exchange. Internationalisation has reinforced the emergence of such hybrid structures, as the original farmer-owners do not want to share ownership rights with outsiders, and as managers usually favour running the foreign business on a IOF basis (i.e., a profit centre). As a result, in some large complex hybrids the cooperative character, in terms of user-control by farmers, is hard to evaluate, and membership commitment may be an issue, particularly as control rights of members have weakened.

Professional structures and policies regarding board composition and member incentives affect performance. In our sample, the typical attributes of "professional" cooperatives like proportional voting rights, professional management, include outsiders in the supervisory board, and selection of directors based on expertise or product representation as opposed to regional origin, all have a positive effect on cooperative performance.

Position in the food chain can be improved by professionalization

In all sectors growth strategies rely to a high degree on autonomous growth, mainly through increasing turnover by upgrading product quality, attracting new members, supporting members to increase production, and diversification in related businesses. Mergers were less stated as important growth strategy, but nevertheless characterise the reality in many sectors. Branding activities performed by cooperatives differ by sector. They are rare in the cereals, sugar, sheep and pig meat sectors, much more common in the dairy and wine sectors. In olives and fruit & vegetables the picture is very diverse.

An analysis on strategy and structure in cooperatives in Mediterranean countries shows that size is not the determining factor of cooperative success; good management is. The introduction of professional management is an important element prerequisite for strengthening the market-orientation and competitiveness of cooperatives. Vertical integration is a necessary but not sufficient condition for better cooperative performance. Natural resources, geography, governance, path dependencies, a shift to value added products, and cooperative leadership issues are equally important. Control of the supply seems to be necessary in order to benefit from vertical integration. The need for the introduction of new ownership structures as well as capital acquisition and management methods is imperative to enable such development. Collaboration of cooperatives with IOFs may lead to better cooperative performance if based on a relatively strong competitive position of the cooperative within the chain. Otherwise, opportunistic behaviour of the IOF is probable.

Federated cooperatives, where a number of first-tier cooperatives own a second-tier cooperative, are not necessarily less efficient. In some cases federated cooperatives are very successful while in other sectors and/or regions they have almost disappeared. The long-run trend, however, seems to be that the federated cooperative model is disappearing or that such cooperatives start to employ activities far away from the farm products of its first-tier owners.

Bargaining associations are important organisation for strengthening the countervailing power of farmers. Currently, these associations are mainly active in the fruit & vegetable and dairy sector, while their role in the post-2015 quota-free market is still unclear. Only in Germany bargaining associations play a role in livestock trading. The biggest challenge to the success and sustainability of the bargaining association is the free rider problem, both external (non-members benefit without bearing any cost) and internal ('cheating' on quality). The relationship between (new) bargaining associations and (existing) cooperatives is a difficult one, and merits further investigation.

In food chains with asymmetric market power, cooperatives provide members and non-members with higher producer prices as long as they handle considerable quantities. In line with the competitive yardstick theory, our analysis in dairy suggests that an overall strong cooperative sector increases prices in the country while at the same time this may not necessarily be attributable to the prices individual cooperatives pay. Rather, a strong cooperative sector makes all dairies pay higher prices, while IOFs pay even a little more than cooperatives (IOFs usually can afford to pay higher prices as they focus on specialties). This

means that also non-members indirectly benefit from the cooperative. Farmers in countries where cooperatives together have more than 50% market share receive 2.50 to 4.50 Euros more for 100 kg milk compared to countries where cooperatives are minor players in the dairy industry. There is also a price-variation-reducing effect of the market share of cooperatives. In pig meat, the other sector for which we did this price effect analysis, we did not find such effects.

In some regions cooperatives are positively viewed as they reduce uncertainty in payments for farmers. Finance of cooperatives is a bottleneck in some regions where risk capital and other forms of equity are not available and the capital markets are inefficient or incomplete, without specialised banks that possess know-how on cooperatives. However this is not the only constraint for emerging cooperatives; often the lack of a profitable business model is an even more important problem.

Farmer preferences for trading in the informal economy may act as a limitation for joining forces in cooperatives. As cooperatives are formal organisation, registering the sales of each member, farmers sometimes prefer to do business with traders. This is more a problem in Southern and Eastern Europe than in Northwest. Although it is expected that over time this phenomena will disappear, as supermarkets prefer to trade with formal organisations, making cooperatives more attractive could induce these farmers to switch to the formal economy. This could be an argument for (continuing) policy support for cooperatives.

Transnationals – a Northwest European phenomenon

Many cooperatives are internationally active in imports or exports. A small group of large cooperatives sources its products from farmers in different countries. We found only 46 transnational cooperatives (i.e., cooperatives with members in more than one country), of which some are federated. Many of these transnational cooperatives act also as international cooperatives, i.e., they also have farmer suppliers in countries where they do not have members. Furthermore, we found 45 international cooperatives, i.e., they have farmer suppliers in foreign countries.

Transnational cooperatives can only be found in a limited number of sectors and in a few countries. Mostly, they are found in dairy and fruit & vegetables, and in the following Member States: Belgium, Netherlands, Germany, Denmark, Sweden and Finland. Thus, transnationals are mainly a northwest European phenomena.

Most cooperatives prefer to internationalise by acquiring or setting up a foreign IOF, and not by merging with other cooperatives. Dilution of ownership and control rights are the main arguments against forming a transnational cooperative, as cited by our interviewees.

Social, cultural and historical aspects matter

The poor performance of cooperatives in some countries (particularly New Member States) has an important social background. Low levels of self-organisation and networking have far more consequences for these countries than simply constraining cooperative development. The issue, then, is how deeply rooted in culture such characteristics and behaviours are.

In the New Member States, overcoming the communist legacy, convincing members by building trust, coping with fundamental collective action problems, often in poor regions with vulnerable rural societies, reflect pioneer activities that resemble early stages of the cooperative movement in other parts of Europe. The issues in the former socialist Member States are diverse and contrasting due to differences in historical backgrounds, pre-collectivisation land reforms, post-collectivisation transformation laws, cooperative traditions and its collective memory, policy streams and the social and cultural context. However, all cases have in common that the impact of the communist legacy persists, as lacking trust was identified as a major obstacle to cooperative development. As shown by the case study on Poland, overcoming this barrier is in the first place the task of trustworthy and skilful leadership. This kind of leadership is the most scarce resource and a real constraint to further development of cooperatives.

In some regions in Bulgaria, agricultural production cooperatives have developed a special type of “ownership” of the villages, in terms of taking responsibility for providing infrastructure, services, rural development aid and a safety net for the poor. In some New Member States, the

agricultural production cooperatives have the characteristics of a worker cooperative, where members bring-in land but are most of all interested in the labour opportunities the cooperative offers.

Human capital is key

Cooperatives need to invest in human capital development, both of their employees and managers and of their current and future board members. In order to attract and keep expertise and skills, they have to compensate their employees and managers well, and may offer board members sufficient compensation for the effort and time they spend on meetings and other activities for cooperative. Just like in other businesses, there is no need to pay (high) bonuses.

In developing human capital general technical and entrepreneurial education and training are necessary, but even more so education and training on the specific organisational and strategic management characteristics of the cooperative.

Although many scholars emphasise that cooperatives, being based on self-organisation, should develop independently from external hierarchies, our findings reveal that there is a strong role for a facilitating state to help farmers in the process of establishing cooperatives. In addition, the state can support the education and training as mentioned above.

Legal issues are not a major hurdle

Legal structures are not a major hurdle for farmers to cooperate effectively and organise their business according to their strategy. In most of the countries there are no major legal problems when cooperatives want flexible arrangements for attracting non-member capital, paying dividend on capital, proportional voting, closed membership, membership exit or inviting external professionals to the Board of Directors or Supervisory Board. But some Member States can provide more flexibility or provide more guidance on how to use bylaws for such issues.

The accountability of the board of directors to members in Greece, Portugal, Spain and the UK is seen as more problematic due to the lack of legal mandates to form a supervisory board, although members can use the bylaws for initiating such a board.

With regard to domestic merger legislation, all Member States do have legal provisions for cooperatives to merge with other cooperatives. Merging a cooperative with an IOF is in some Member States more difficult. There are no legal barriers in merging cross-border, notably through the establishment of a SCE. Yet, the SCE is not used by agricultural cooperatives as it has no added value for them.

The way cooperatives are treated by the tax authorities of most Member States seems to facilitate their growth. Cooperatives are treated as an extension of members' farms. Consequently, surpluses (money earned from selling members' products) return to members in cash or held in individual accounts by the cooperative are taxed only at the farmer level (single taxation principle). Profits, that is, money earned from selling non-members' products, are taxed at the cooperative and, if distributed to the members, at the farm level. However, there is also a considerable number of Member States in which cooperatives are taxed like IOFs.

Competition law is relevant

Cooperatives are not exempted by competition law. However, the EU Court of Justice, assessing the application of Article 101(1) of the TFEU to farmers' cooperatives, has clearly recognised in several occasions the pro-competitive effect of cooperatives and has established that the prohibition principle of Article 101(1) does not apply to agreements that contribute to the improvement of the competitive conditions of the markets. However, the interpretation of what constitutes competitive conditions of the markets differs substantially between farmers, who feel exploited by large retail customers, and competition authorities, who seem to be mainly concerned about consumer benefit.

Cooperatives and producer organisations perceive legal uncertainty in competition law and report high costs due to burden of proof. In F&V there seems to be conflicting policy objectives between the CMO (bundling) and competition law. Some other OECD countries (e.g., the USA)

have more exemptions for cooperatives – albeit under strict conditions – in competition law to rebalance market power.

Cooperatives are relevant for rural development, but this is not their primary objective

The links between cooperatives and rural development are manifold. Cooperatives are more likely to be set up in remote areas where farmers face high transaction costs due to market failure. Being far away from consumer markets, having little information on final demand, and facing monopsonistic or oligopsonistic market structures, farmers in these areas need cooperatives to provide the inputs that would be available otherwise and to provide them with bargaining power in their output markets. Cooperatives in such regions are often important employers and more generally contribute to regional economic development. In many cases the activities of these cooperatives go hand in hand with pursuing public objectives such as the development of human capital, improving competitiveness and environmental protection. In some cases cooperatives build their business strategy even on regional characteristics and social processes, resulting in, for instance, regional or fair trade-type of products and services or links with tourism.

Cooperatives are in the first place businesses. Activities that do not fit in the business model of the cooperative are not taken up or are terminated sooner or later. Also in the New Member States the role of the cooperative is now business-oriented and totally different from the situation under socialist rule. We came across one important exception: in some regions in Bulgaria (see above) the political and administrative governance is so weak that the villagers depend on the cooperative for many public functions.

Many supportive policy measures, but impact is unclear

In total more than 300 European, national and regional policy measures were identified. Cooperative legislation, competition rules, inducements (money transfers) and financial incentives were among those reported most often. There are large differences in the policy measures between Member States. Support for capacity building and technical assistance are much less used as policy measures, and when capacity building is used, directly improving the position in the food chain (e.g., with marketing knowledge) is a more important goal.

There are no clear links between the (current) support measures for farmers' cooperatives and the performance of cooperatives in terms of market share. Also in other OECD countries (Australia, Canada, New Zealand, Norway, Switzerland, USA) the absence of policies that support cooperatives can have positive as well as negative effects. A flexible cooperative law is helpful to develop internal governance. In addition, tax systems seem to be important as well as anti-trust (competition) rules. The latter do not have to favour cooperatives, but they can be problematic if they do not take into account the specific nature of cooperatives. Policy coordination is important, especially in federated countries, not only between the regional and central level but (for countries as Spain) also between neighbouring regions as cooperatives work across regions.

Cooperatives also benefit from the direct payments of the agricultural policy and the national energy policy (East Germany), especially agricultural production cooperatives. Reforms of the Common Agricultural Policy can have very different effects on successful cooperatives. Besides some negative reactions, we found many positive dynamics generated by CAP reform, e.g. in sheep, wine and sugar cooperatives.

10.2 A reflection on countervailing power

Given the conclusions drawn thus far and the objectives of this study, the countervailing power issue resurfaces. Are cooperatives able to countervail the excessive market power of their customers along food supply chains and thus redistribute income in farmers' and society's favour? In order to address this question, we first focus on power imbalances in food supply chains and then use our conclusions to reflect on the question.

The food supply chain is characterised as imbalanced because of the significant concentration in the food processing and, particularly, retail. It is estimated that the majority of

the European food is bought by the retail through about 110 buying desks (Grievink, 2003), where perhaps about 3 million farmers produce three quarters of our food (EU SCAR, 2012). It has been much easier for the retail (and food processors) to gain economies of scale than for farming, where production factors are less mobile. Given current technologies, the average farm size is still lagging behind the optimal level. But even the (technically) optimal farm size is still much smaller than the size of its transaction partners in food trading, processing and retail.

Although the return on investment is higher in retail and food service than in farming, there is a heavy competition between retail brands, in which price is an important aspect for many consumers. This reinforces concentration (the cost of buying 50,000 tons is more or less equal to that of 5 tons, so cheaper per kg, and a similar reasoning holds for marketing and R&D); it puts pressure (for bulk orders) on earlier stages in the chain. As some are able to deliver at these prices (costs vary significantly in agriculture due to, among other reasons, differences in scale) and production is, at least in some years, abundant, prices are under strong downward pressures - as they did in the last 200 years. For farmers this is an unwelcome signal that markets put pressure towards more restructuring and enhanced efficiency.

The emphasis by consumers on price has also not been very helpful in producing food with methods that optimally respect the environment, animal welfare, working circumstances (e.g. of immigrant workers) or even food safety. There are also complaints that the pressure on prices goes hand in hand with unfair commercial practices, such as late payments and other forms of unfair trade practices. From this perspective, consumers pay, at least in some countries, too little for food. Of course, increasing the prices received by farmers will not address such issues automatically. On the other hand, such problems should not be used as an excuse for relaxing competition rules. Nevertheless, in many regions, consumers have altered their buying behaviour by turning to quality food and environmentally friendly products - an opportunity for positive change.

Given this situation of imbalanced supply chains the question is what the role of cooperatives is, or could be, in reducing the effects of the imbalances in the food chain for their farmers. Our study found mixed results. We have no results showing that individual cooperatives, including large transnationals like FrieslandCampina and Arla Foods in the dairy sector, have sufficient market power to balance the power of the retail giants (although in regional markets they may hold a strong position). As the retail supply market for the most part is a European market, cooperatives face strong competition from other (foreign) cooperatives and from IOFs. The transparency that cooperatives apply in the pricing of their main raw material (e.g. milk or sugar) is beneficial for the bargaining power of retailers as it provides valuable market information. Where cooperatives pay prices not on delivery but in several rounds as in marketing pools to deal with volatile prices and provide liquidity to farmers, it is not wise to force them to be more transparent and quote prices on delivery.

One should also ask another question: What would be the consequences for farmers if cooperatives would no longer exist? To answer this question, one only needs to go back to the conditions prevailing before cooperatives were formed. In most cases, the farmers were in despair.

On at least two aspects the role of the cooperative is proven to be positive. One is the fact that in regions with a large market share for cooperatives, prices (for dairy) are higher, in line with the competitive yardstick theory. Non-cooperative members benefit from this as they also receive a bit higher price for products delivered to IOFs producing specialities, to compensate them for the risk that IOFs move to another, cheaper region or more profitable industry. A second aspect is that cooperatives offer payment guarantee to their members, which is very important for farmers in most regions.

The situation of cooperative still being rather small compared to their retail counterparts also means that farmers have to live with cooperatives becoming larger and with an on-going loss of influence of the individual member. There are cases where this seems to be possible without losing the cooperative identity.

Moving from the current role to potential contributions of the cooperative, there are different roles for the various types of cooperatives (see the clusters identified in Chapter 2).

The **agricultural production cooperatives** (like in the east of the Union) and different types of service cooperatives (for the joint use of machinery or for farm help, etc.) can play an important role in improving efficiency in agriculture. More efficient use of machinery and buildings, as well as some level of specialisation between farmers help. Such cooperative experiences can also help to build trust and is a basis for cooperative action in the next stage of the supply chain.

Bargaining associations seem not only a tool to strengthen farmer bargaining power, they also are an efficient vehicle to reduce transaction costs in the supply chain and improve coordination of operations, particularly on quality aspects. A food processor has larger costs when doing business with 1000 individual farmers than with one bargaining association representing those 1000 farmers. If a bargaining association is able to organise the collecting of a large quantity of uniform product quality, it has an attractive business proposition. Bargaining associations not only operate in selling farm outputs, they also are an efficiency enhancing tool for the joint purchase of farm inputs.

Niche cooperatives focus on consumer segments that are willing to pay for specialty products such as, for instance, regional or environmentally friendly, healthy or 'slow' food. Marketing and building of the brand is of course very important in this case. Supermarkets or food service companies can be interested, especially if they get a certain exclusivity provision that helps them make a difference with their retail format. Co-production and co-innovation are probably more important here than countervailing power. For some products in some cities there are signals that the combination of internet shopping and inexpensive home delivery of parcels is offering a new channel to reach the consumer.

The large **specialised food processors** and the large transnational **agribusiness cooperatives** have to keep fighting at two fronts. The easiest one is perhaps that they have to be as efficient as competing IOFs. As the return on investment in first processing is not very attractive for listed companies, some of them tend to leave the industry. We have seen that in some markets this effect is bigger than the effect of cooperatives becoming IOFs. Farmers have to realise that this asks for investments in their cooperative, although some of the required capital may be invested by outsiders, such as in hybrid constructions. Both additional member investments and for members accepting outside investors (which may dilute member control) are challenges for membership commitment. The required additional effort of the cooperative leadership in strengthening member commitment is comparable to the effort that was needed for trust building via direct communication at the time the cooperative was established. In such large professional organisations, that adds to the cost of doing business. The even more difficult front is collaboration with the retail. Here market size could help, also to reduce fixed costs per unit, and therefore it is to be expected that mergers between cooperatives will continue, especially in sectors where supply and demand are changing (e.g., due to policy reforms like in sugar or dairy). This will be increasingly a cross-border process with headquarters and research labs on the move, as several of these cooperatives have few options left for mergers in their home country. Setting up a federated cooperative (or an APO in fruit and vegetables) could be an intermediate solution.

Another option for such cooperatives is to be a very efficient producer and produce for the private labels of retailers. That reduces investment costs in branding, and the close relationship between farmers and their cooperative could help in minimising transaction costs.

In the next chapter we elaborate on this reflection and summarise the resulting operational implications for farmers, cooperatives, policy makers and research.

11 Operational conclusions

This study is first of all a fact finding investigation into the state of agricultural cooperatives in the imbalanced food supply chains and into relevant policy support measures. We therefore try to be modest in providing detailed policy prescriptions for farmers, cooperatives and policy makers. However, as our main conclusions are rather close to what the academic literature suggests, we address in this last chapter a number of issues for the agendas of the stakeholders that follow from our analysis.

11.1 Farmers, cooperatives and their professional associations

Farmers interested in starting a producer organisation, bargaining association or cooperative are advised to pay sufficient attention to the issues of leadership and human capital. It requires social, economic and organisational skills and resources, and sufficient time and capacity for building the organisation. Legitimate institutions such as cooperative legislation and cooperative traditions can greatly support this process of setting-up a new collective action organisation.

Once the organisation is established, members and directors are advised to pay sufficient attention to professionalization. This includes developing and updating a good strategy with a business model that generates added value. It also applies to internal governance, where members of the board of directors need to have the knowledge and skills that are required for choosing proper strategies. Further, when directors delegate strategic and operational decision-making to professional managers, they need to have sufficient skills and knowledge to control them effectively. Thus, a growth and marketing strategy of the cooperative may not only require a professionalization of the management – for instance, acquiring more marketing skills – it may also require strengthening the control capacity of the board of directors and supervisory board.

Our study is in line with current literature on restructuring corporate governance in cooperatives, which analyses the trend towards more differentiated board models that may have a differential impact on member control (e.g., Bijman et al., 2012). Although governments can support human capital and the development of cooperatives in a market economy (see next section), the professionalization of management and boards are primarily a responsibility of the farmers and cooperatives themselves, and a prerequisite for state support to be effective.

Large cooperative food processors and (international) agribusiness cooperatives are professional to the extent that they have access to top management markets as well as management consultants. But one issue that comes out of this study, and is not always part of the regular manager's skills and knowledge, is that membership involvement and commitment is a challenge that will only grow in importance with more international mergers to come and deserves an important place on the agenda of the board of directors of such cooperatives.

Professional associations of cooperatives (like Copa-Cogeca and its national members) could help their members (especially the smaller ones) by providing access to knowledge and best practices for professionalization, especially in an international context, making use of support measures where available (see next section). As this study advocates flexibility in cooperative legislation to promote innovation in internal governance, this opens also a role for guidance on this topic, e.g., with model bylaws for typical cooperatives at the national level.

11.2 Regional, national and European policy makers, including competition authorities

Regional and national governments responsible for cooperative legislation could use this study as well as recent special studies on the legal aspects of cooperatives to evaluate current legislation. Although, on average, legal issues are not a major hurdle for farmers to cooperate effectively and for cooperatives to develop, we also found that performance is clearly influenced by internal governance. Governments should check if flexibility and guidance in their legislation

is optimal. We refer to the background reports for details, but point out here that in some regions and countries at least a check is needed on cross-regional collaboration and mergers of cooperatives (especially in federated countries) and on the issues of supervisory boards, professional management (including external board members) and outside finance. A similar check concerns tax policies. Finally, the European institutions should reflect on the future relevance of the SCE Statute which is currently not considered as useful for agricultural cooperatives.

Cooperatives are on the radar of (national) competition authorities, and this will intensify with more mergers to come. However, cooperatives and producer organisations experience legal uncertainty in competition law and report high costs due to burden of proof. Clear rules and regulations are in everybody's interest, even if cases are always specific (and if so, full explanation of considerations in rulings helps to build up case law). In principle, cooperatives are contributing to developing and improving the operation of markets. Some other OECD countries (e.g., the USA) have more exemptions for cooperatives in competition law to rebalance market power.

Support measures

Agricultural cooperatives and producer organisations show positive externalities and produce public/semi-public goods. Contribution to rural development goals, particularly in disadvantageous areas and/or declining industries, is prominent among such contributions of cooperatives. Besides income, employment and better market conditions (also for non-members in regions with a high market share of cooperatives) as well as environmental effects, there is the contribution to human capital and social inclusion. There are also examples where new bargaining associations or cooperatives showed innovative behaviour, for which farmers sometimes had to fight in or even break away from larger cooperatives as, e.g., organic or regional products did not fit in the business model. These all merit the attention of policy makers and can be a basis for designing support measures.

Besides enabling cooperative laws, supportive (single) tax legislation and clear and fair competition rules, additional policy support should focus on human capital building among members, directors and managers of cooperative, but also among legislators and administrators dealing with agriculture and the food chain. In general, support measures and policies targeting agricultural cooperatives have a higher chance of achieving policy objectives when they take into account organisational, regional, historical and other particularities. Of course, sometimes even after taking into account the aforementioned differences, there still remains significant variance among Member States. Coordination between different governmental levels and policies is equally important. It is clear that better impact assessment of policies would help in evidence-based policy making.

Agricultural producer organisations and agricultural cooperatives have, undoubtedly, benefitted from the Common Agricultural Policy and its several reforms. The EU policy, recognizing the important role of agricultural cooperatives for the rural EU, has been supportive in several ways. The Common Market Organisation of particular agricultural products has been crucial in enabling a more efficient coordination of the respective supply chains, and this supports current policy (proposals) in fruit & vegetables and dairy.

FEADER funds have been instrumental in agricultural cooperatives' attempt to build and expand their processing and distribution capacities. However, FEADER funds are only available for small and medium-sized firms, which functions as a disincentive for mergers among small cooperatives into larger units. These merger processes are desirable from the perspective of strengthening the bargaining position of farmers in the food chain. Agricultural policies (and some national policies like those on renewable energy) can influence cooperatives considerably and this should be taken into account in impact assessment by policy makers and researchers. There are many examples where cooperatives benefit from these policies as well as their reform. But there are also examples of negative effects or mixed effects (in the sense that policy measures are not coherent).

Need for capacity building and technical (organisational) assistance

There is one type of policy measure that is according to our findings not often used, and that in the literature is a topic of debate: to what extent should national governments and the EU be involved in capacity building and technical and managerial assistance that support the development of human capital in cooperatives. Although many scholars emphasise that cooperatives, being based on self-organisation, should develop independently, our findings reveal that there is a strong role for a facilitating state to help farmers develop organisational skills, and mostly in the New Member States.

Farmers in smaller cooperatives and especially those in new emerging cooperatives often depend also on outside-help, although there are impressive examples (like in Lithuania) where members managed on their own. Particularly young farmers as potential future board members in small and large cooperatives could benefit. In northwest European cooperatives, agricultural development in the 1960s – 1970s benefitted from leadership development of young farmers, among others in American exchange programs. Similar exchanges could be set up in Europe. Large cooperatives (including rural cooperative banks) can play a positive role of setting examples or even mentoring. We became aware of an interesting social “tutelage” between a French and a Romanian cooperative, not linked to any business opportunity. Similar examples of tutorship exist between cooperatives from Europe and cooperatives in developing countries. Transnational and international cooperatives could perhaps be involved, too. Although they are not interested in having foreign members, in the long run they could benefit from good functioning bargaining associations in their host countries to optimise the supply chain. In some regions also banks and policy makers as well as the agricultural education system could benefit from more know-how on cooperatives. Extension or advisory services and research could play a role too in such a program for facilitating capacity building and technical assistance. Current European policies like the CAP 2nd pillar, the proposed so-called Operational Groups in the European Innovation Partnership facility of the new CAP and other EU support measures seem to be close enough to incorporating these suggestions.

A monetary incentive to organise, professionalise and innovate (like in the current CMO for fruit and vegetables) could support capacity building. However, such a shift from direct payments to farmers towards payments to producer associations (in food production or nature conservation) can also have negative aspects like subsidy-dependence or making life more difficult for existing cooperatives.

11.3 Further research and statistics

For future studies it would be helpful if more data on cooperatives would be available. As we concluded in Chapter 2, many aspects of cooperatives are not well covered in statistics. For conducting further in-depth research on the interaction between cooperative performance and policies, the EU is advised to build a reliable database on agricultural cooperatives in the 27 Member States. Such data would improve policy assessments, knowing that some cooperatives are much more influenced by CAP reform policies (positively and negatively) than we usually learn from impact assessments. However, we acknowledge that dynamic effects are extremely difficult to model in a quantitative way.

Suggestions for further research that result from our study, include the following issues.

- What drives the success of exemplar cooperatives in countries/regions where the majority of cooperatives have not been very successful?
- How do the various internal governance models adopted by agricultural cooperatives in EU countries affect cooperative performance?
- What are the evolutions of, and economic roles played by, agricultural cooperatives in key agricultural/food sectors in the EU?
- How can cooperatives combine objectives of regional development with a stronger market orientation?
- How to (new) bargaining associations affect the performance of (existing) cooperatives?

- How does national and EU legislation affect the establishment and development of bargaining associations in the European F&V sector?
- What are the differences in structure and performance between cooperatives (as pure user-owned firms) and firms owned by producer associations and farmer unions (as member-owned firms).
- Can cooperatives benefit from the growth in private label sales of supermarkets, growth of food service and growth of internet-sales?
- How can elements of the US system of anti-trust exemption for cooperatives (under the Capper Volstead Act) be incorporated usefully in EU legal frameworks?
- How do the economic, social and psychological conditions (including issues of trust) in the agrifood sector in the New Member States affect the establishment and development of cooperatives?

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Annex 1. Background reports

Country Reports	
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