Special Issue: Pathways to Rural Economic Development in Transition Countries: The Role of Agricultural Cooperatives

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EDITORIAL

This special issue of the *Journal of Rural Cooperation* contains a selection of papers delivered at the international conference, Rural Cooperation in the 21st Century: Lessons from the Past, Pathways to the Future, held June 14-17 on the campus of the Hebrew University of Jerusalem, in Rehovot, Israel. Conference attendees included scholars in the field of rural cooperation from Israel, North America, and Western and Eastern Europe. The papers chosen for collection in this volume represent a diverse set of methodologies and regional foci. Their common theme, consistent with the focus of the conference, is enhancing our understanding of the role of cooperatives in agricultural and rural development, and devising strategies to improve their effectiveness.

Finkelshtain and Kachel explore an important issue in cooperation. Granting agricultural producers the right to market their products collectively will typically require an exemption from the home country's antitrust laws. This exemption has caused some to raise concerns about farmer cartels that could exercise market power over downstream users. However, if producers sell into concentrated downstream markets, as is the typical case today, cooperatives may serve to countervail downstream buyer power, and, thus, improve economic welfare.

Finkelshtain and Kachel develop an innovative methodology to study the interplay of these forces for the Fish Growers Cooperative in Israel, an organization formed to enable Israeli aquaculture producers to market their production jointly. They estimate derived demand functions for the major fish species produced in Israel and approximate long-term supply functions based on production costs in different regions in Israel. These functions provide the basis for simulating equilibrium outcomes of different market structures, including a producer cartel, a downstream monopsony, and a benchmark outcome of perfect competition. To account for the possibility that cooperation provides growers with countervailing bargaining power against an imperfectly competitive marketing sector, they simulate the outcome of a cooperative Nash bargaining game.

Results indicate that the Fish Growers Cooperative did not behave like a cartel and marketed quantities close to the competitive equilibrium. However, imperfect competition in the fish marketing sector may, unchecked, cause a significant decline in producer surplus, consumer surplus, and total welfare. Cooperative marketing of producers, by acting to countervail this market power, can increase producer surplus and total welfare.

Fulton and Larson present a thought piece on the evolution of cooperation in Canada. Canadian cooperatives have undergone significant turmoil over the past 10-15 years, with key grain, dairy, and poultry marketing cooperatives converting to investor-owned forms through mergers or takeovers. Fulton and Larson trace the demise of these cooperatives to management problems and lack of adequate oversight by their boards of directors. In particular, the authors point to managerial hubris and overconfidence as the decisive factors that led these cooperatives to finance extensive capital expansions with debt without undertaking the detailed market analysis that might have suggested a more cautionary approach. A long-held concern is that cooperatives' boards may be less effective at overseeing and disciplining management than boards of investor-controlled corporations. Fulton and Larson present compelling evidence of the disastrous consequences that may result when overzealous co-op managers operate without adequate controls or oversight.

Mérel, Saitone, and Sexton focus on the role of agricultural marketing cooperatives in modern food markets that emphasize product and firm quality and differentiated products. Various traditional cooperative business practices are not conducive to success in meeting consumers' demands for quality, and the authors discuss and evaluate these limitations which have led to pessimism regarding the future of cooperatives. However, they also demonstrate advantages, relative to investor-owned firms, inherent in some traditional co-op practices, such as revenue pooling.

Mérel, Saitone, and Sexton further argue that our ability to understand cooperatives' role in these modern, differentiated markets is restrained by the fact that most economic models of cooperatives presume that the firm produces a single, homogeneous product. Thus, they propose and illustrate appropriate modeling frameworks to study cooperatives' performance in differentiated-product market settings, including comparing the performance of open- and closed-membership cooperatives in competition with an investor-owned firm in a market with horizontal product differentiation.

In western economies agricultural cooperatives are organized by producer initiative. However, in other settings they are set up by government through a "top-down" approach. Golovina and Nilsson explore the top-down approach to cooperation for 21 supply and marketing cooperatives organized recently in the Kurgan region of Russia. The authors conducted interviews with 141 members of these cooperatives at two distinct points in time (early and late 2008). They sought to test the hypothesis that members' attitudes towards cooperatives improve as they acquire experience in working with them.

The question is important because it sheds light on whether government can be an impetus for sparking cooperative action through a top-down approach that can then eventually lead to the cooperatives evolving into the classical model of member ownership and control. The findings, unfortunately, are rather strongly negative in regard to this key question. The members' experiences from the top-down organized cooperatives made them uniformly less positive towards cooperatives. The results lead the authors to question whether top-down organized cooperatives can be a successful tool in transition economies.

Davidovich, Heilbrunn, and Polovin present an intriguing hypothesis regarding the Israeli Kibbutz movement. Kibbutzim have traditionally been egalitarian organizations, based upon equal sharing of the collective resources. In the last decade, however, more than half of the Kibbutzim have changed towards a less cooperative system characterized by financial payments based upon members' specific contributions to the Kibbutz's enterprises. The conventional wisdom is that these differentiated-payment Kibbutzim should feature greater entrepreneurship and risk-taking activity than the traditional collective enterprises because innovators can capture the rewards to their entrepreneurship. However, the authors' propose a hypothesis that supports an opposite outcome. If risk aversion as well as inequality aversion (aversion to an unequal income distribution) is assumed, then higher equality among participants can motivate people to make risky efforts.

The division of Kibbutzim between the traditional collective approach and the new individual-oriented approach provides a basis to test the competing hypotheses. Results of an empirical study of 58 Kibbutzim show that individualistic Kibbutzim engaged in less risky activities than their collective-oriented counterparts, providing support for the authors' hypothesis that greater equality motivates members to take on riskier challenges.

McKee, Shaik, and Boland provide an empirical analysis of a sample of 58 farm supply and grain marketing cooperatives operating in the U.S. northern prairie. In response to financial stress these cooperatives have faced increased working capital requirements. The sample cooperatives were observed on average to have reduced liquidity from 2002 to 2006 and to have become reliant increasingly on debt capital. The authors hypothesize that managers of the most profitable cooperatives sacrificed liquidity and increased leverage in order to achieve profitability targets. Their econometric model specifies profitability (gross margin relative to assets) as a function of liquidity and solvency ratios, as well as control variables. The model was estimated on a panel data set for the 58 cooperatives for years 2003-07. Results demonstrate an inverse relationship between profitability and liquidity and also solvency. The authors conclude that the results support a hypothesis of managers using financial resources in ways which tend to decrease profitability.

Together, the papers in this volume provide insights into strengths and weaknesses of cooperatives and tools and approaches that may enhance their effectiveness moving forward. I hope the special issue will provide a useful reference for scholars in the field and be a stimulus to further research.