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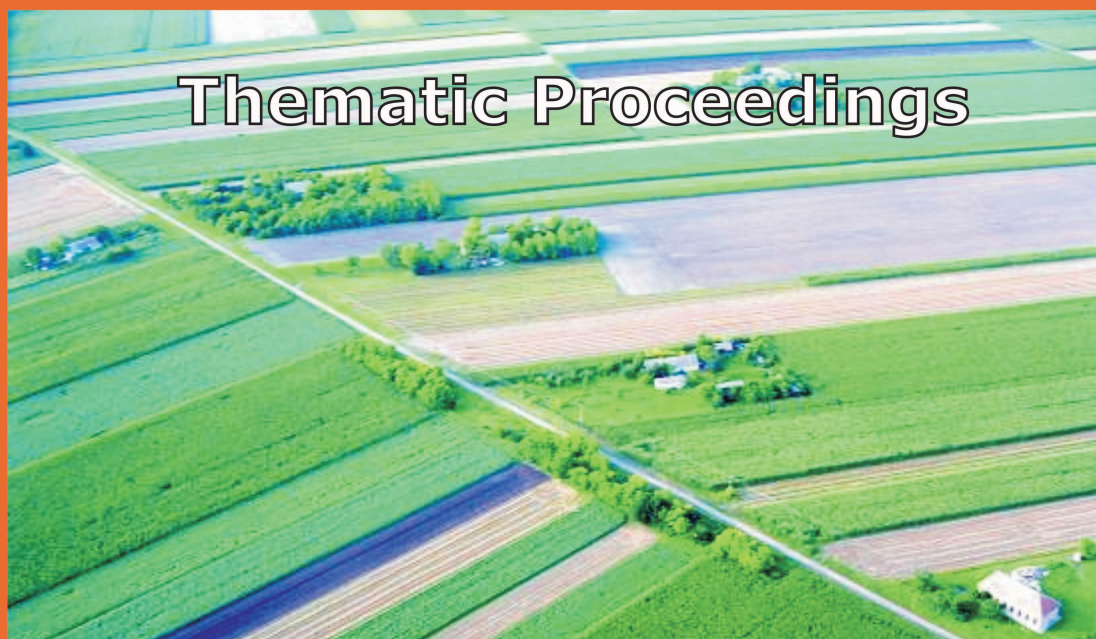
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Miladin M. Ševarlić



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THE NEW GENERATION CO-OPERATIVES AND POSSIBILITY OF THEIR IMPLEMENTATION IN THE COUNTRIES IN TRANSITION

Miladin M. Ševarlić¹, Branka Krivokapić Skoko², Marija M. Nikolić³

INTRODUCTION

This paper consists of three parts. The first part outlines the characteristics of NGCs, defines their activities, and explains differences from traditional cooperatives. It also discusses advantages that NGCs have in promoting the development of local rural communities. The second part analyses the role of agricultural co-operatives in transition countries using Serbia as a *case study*. Finally, we provide some preliminary evaluation of the expected implications which NGC might have in transition countries.

NEW GENERATION CO-OPERATIVES

New Generation Co-operatives can be seen as an example of co-operatives adapting their structure and strategy to reflect many of the changes occurring in the industrialised agriculture, such as an increased vertical integration and co-ordination in farm production, new technology, and globalisation. The main focus of NGCs is on value-added products rather than marketing raw commodities or supplying farm inputs as it is the case of traditional co-operatives. NGCs are structured to facilitate the capital investment required for successful value-added food processing. The model of NGC is characterised by large up-front capital payments by prospective members, tradeable equity shares linked to delivery rights, and closed or restricted membership. This model also implies far-reaching vertical integration, giving farmers larger earnings through selling processed products instead of raw products. New Generation Co-operatives are involved in

¹ Dr. Miladin M. Ševarlić, Full Professor, Department of Agricultural Economics, Faculty of Agriculture, University of Belgrade, Serbia, 11080 Belgrade – Zemun, 6 Nemanjina Str.; Phone: +381-11-2615-315, Ext. 403. e-mail: milsevar@eunet.yu;

² Dr. Branka Krivokapić-Skoko, School of Marketing and Management, Faculty of Business, Charles Sturt University, Panorama Avenue, Bathurst, 2795 NSW, Australia ; Phone: + 61- 2 -63384428, e-mail: bkrivokapic@csu.edu.au;

³ Graduate engineer Marija Nikolić, Teaching Assistant, Department of Agricultural Economics, Faculty of Agriculture, University of Belgrade, Serbia, 11080 Belgrade – Zemun, 6 Nemanjina Str.; Phone: +381-11-2615-315, Ext. 403. e-mail: marijahnikolic@yahoo.com;

highly differentiated production and focused on achieving dominant market position in small market segments, such as regional markets, specific consumer groups, speciality products such as organic products. They focus on large scale operations, with a high investment in production and marketing and tend to occupy dominant position in segmented markets. They also tend to be involved more in highly differentiated markets (Gunnarson, 1999; Nilsson, 1997; Fulton, 2000; Fulton and Gibbins, 2000; Plunket and Kingwell, 2001; Olson et al, 1998; Stefanson and Fulton, 1997).

New generation cooperatives (NGCs) have several features that distinguish them from more traditional cooperatives. These features are:

- (a) delivery rights that are tied to the level of equity invested
- (b) closed membership
- (c) higher level of initial equity investment
- (d) transferability and the opportunity for appreciation or depreciation in the value of delivery rights.

(a) Essentially, delivery rights shares act as a two-way contract between the producer-members and the cooperative. They obligate the producer-members to deliver a certain amount of farm product to the cooperative each year, and in turn they obligate the cooperative to accept delivery of the product. The use of delivery rights assures producers a market for their product, and assures the cooperative a steady source of its primary input. The shares that allocate delivery rights are separate from membership shares. Each individual producer holds only one membership share, but can hold more than one delivery rights share. Voting rights are attached to the membership share, and therefore each producer only has one vote in the cooperative's affairs, regardless of how many delivery rights shares he may hold. This is consistent with the democratic principle of one member, one vote that characterizes most cooperatives.

(b) In contrast to many traditional cooperatives that typically accept new members on a continual basis, membership in new generation cooperatives is restricted once the targeted amount of delivery rights shares are sold. Once that occurs, new members will only be allowed if an existing member wishes to sell some of his delivery rights shares to another producer.

(c) Because of the presence of delivery rights, the initial equity investment required from producers is higher for a NGC than that found in most traditional cooperatives. NGCs typically raise between 30 and 50 percent of their total capital requirements from the sale of equity shares (Harris, Stefanson and Fulton 1996). Producers must pay for the right to deliver their commodities to the cooperative and in order to participate in the cooperative's value-added processing, producers must provide up-front capital by purchasing delivery rights. The NGC usually sets

a minimum required number of delivery rights shares that a producer must purchase in order to be eligible for membership. Because the members invest a significant amount of equity and are obligated to deliver product, they tend to remain more committed and involved in a NGC than they might be in a traditional cooperative.

Also, in comparison to a more traditional cooperative, the NGC receives a higher level of equity financing at the start of its operations. The NGC is therefore in a position at the end of the year to return a greater portion of its patronage refunds in cash to its members, rather than retain them in the business as additional equity financing. In other words, since the members invest a significant amount of capital up front, most of the net earnings generated are returned to members at the end of the year rather than used as equity financing for the business. If the NGC decides to expand its operational capacity, then it issues more delivery rights shares, which provide the necessary equity financing for the expansion.

(d) As mentioned, members of the cooperative are typically allowed to transfer their delivery rights shares to other members or other producers who wish to become members, subject to board approval. The price of the shares in these situations is negotiated between the member who is selling and the producer who is buying. The price of the shares will therefore fluctuate according to the performance and earning potential of the cooperative. If the cooperative is performing well and the buyer perceives strong earning potential from owning the delivery rights, then he may offer a price that is higher than that originally paid by the member. The member would therefore be able to realize a gain from the appreciation of the share value. Alternatively, if the buyer perceives that the earning potential is weak, then the share might have decreased in value for the member.

These features appear to generate a considerable sense of ownership, control, and commitment amongst farmers-members who are now able to capture returns from further processing of their farm products and to achieve a higher profit on value-added products. Thus, the formation of NGCs is intended to raise income for the individual farmer and, consequently, to generate additional economic activities for the benefit of rural communities. A number of authors have considered the model of NGC as having a rather positive role in rural development and as particularly appropriate for the rural communities experiencing population decline and economic stagnation, and where viability of both farm and non-farm businesses is at risk. It is expected that farmers-members can maintain a control over their operations, reduce risk, stabilise income and secure markets for their products (Stefanson and Fulton, 1997; Stefanson et al. 1995; Livingston et al, 1998).

In light of the enthusiasm over the success of NGCs as a tool for rural development, it is also necessary to refer to the potential pitfalls for NGCs as identified in the literature, and which require caution and detail consideration in practice. The case studies carried out by (Leistriz and Sell, 2000; Fulton and Gibbings, 2000; Livingston et al, 1998; Waner, 2000) and more general sources (Cobia, 2000; Stefanson et al, 1995) show that important drivers of the economic success of NGCs are: (1) external factors in forms of public sectors support; (2) clearly identified mission; (3) adequate planning; (4) use of advisers and consultants, particularly facilitators and co-operative development specialists. Furthermore, the NGC model should not be applied to the businesses that do not incorporate high members' equity investment and the strategy of two-way delivery contracts. Apart from the strong membership commitment through delivery contracts and investment, some common characteristics of the unsuccessful NGCs the literature identifies: (1) lack of leadership (2) lack of membership commitments, (3) inadequate management, (4) failure to identify and minimize risk, (5) lack of technical assistance, (6) lack of capital, and (7) inadequate communication.

COOPERATIVE MOVEMENT IN COUNTRIES IN CENTRAL AND EASTERN EUROPE: BETWEEN TRADITIONAL AND NEW COOPERATIVES

Transition from socialistic to market model of economy in countries of Central and Eastern Europe have caused „transition shock” in cooperative movement and non-readiness of cooperatives to adapt in quick and efficient manner to new economical changes under influence of external (globalization and liberalization) and internal factors (privatization of state or, in Serbia - public¹ property, competitiveness of private agribusiness companies).

Beside certain differences in premises of major number of authors (Hillbom I., 1998; Harris A. et al, 1998; Randelović V, 1999; Bartus P., 1999; Bekkum van O., 1999; Zakić Z., 2000; Fulton M., 2001; Chloupkova J., 2002; Holmstrom, Ševarlić M, 2000; Bogdanov N., 2005; Ševarlić M., 2005), cooperative movement in process of transition had mutual characteristics for all transitional countries and certain specifics in Serbia. These differences can be systematized in following statement:

- new political elite in most state departments had no appropriate knowledge on position, role and significance of cooperative movement, and some of them had

¹ Public property is specific form of property that was introduced in economically-political system of Serbia (and other countries created at the end of 1990's on territory of ex SRF Yugoslavia) after 1953 as form of “collective workers' property”.

extremely negative attitude and have considered cooperative movement „recidivism“ of devastated socialistic social-economic system. Cooperative movement therefore had second-grade significance comparing to other sectors of economic transitional changes, where in focus was privatization of public property;¹

- impact of cooperative unions on ministries of agriculture, finance and other state sectors has been significantly reduced, particularly in process of adopting new system laws for adapting to market economy, where specifics of cooperative organization and work have not been in totally respected;²
- in reconstruction of cooperative sector, process of determination direct titular was challenged. Cooperative estate was being transferred to some ex and current members of cooperatives or at their cooperative unions, with intention to devastate cooperative estate and to transfer it to state property or to submit it to privatization;³
- privatisation of food industry – although cooperative members, workers and cooperatives had invested significant resources – have been done without influence and right of claim of proportional part of capital for cooperatives;⁴

¹ In transition so far in Serbia public property in cooperatives was practically excused from privatisation, with comment that new *Law on cooperatives* is expected that would regulated all those questions. However, from 2000 there had been several attempt of adoption of new cooperative law, but all activities ended on draft law given by ministries and so called public dispute on these draft laws – without their finalisation and adopt in Parliament.

² Adopting *Law on banks* minimal institutional share was set down on 5.000.000 US \$ in Serbia, and none of the credit cooperatives could not fulfil this precondition. Therefore even the oldest *Railway credit cooperative – Belgrade* with about 50.000 members stopped to exist. At the same time, introducing *VAT-value added tax* members of housing cooperatives lost their tax perks for provision of structural materials and with that they lost interest to be members of housing cooperatives.

³ In Serbia were created administrative and political obstacles to register cooperative estate as cooperative, but it was insisted on registration as public property. In such manner this estate could become submitted to privatization, which was indeed the process characteristic for most of the countries formed on the ex SFRT territory. At the same time, some agricultural companies that were formed on cooperative estate during the socialistic economic system, tried to reconstruct as cooperatives in order to escape privatization sale and to save cooperative estate in favour of large part of members of local communities.

⁴ Only exception from all the countries created on ex SFR Yugoslavia territory was Slovenia, where 40% of capital value estimated in privatization process of food industry have been transferred to cooperative unions, with rationale that this was rated contribution of cooperatives and cooperative members to construction of capacities for processing agricultural products.

- inadequate position of cooperative movement in transitional period significantly contributed and human resources devastation – as less interesting employers for agribusiness managers;¹
- Transition from socialistic to market economy were followed by many bankruptcy of agricultural companies and agricultural cooperatives, where significant part of cooperative estate were devastated on two grounds:
- in case of bankruptcy of agricultural companies cooperative estate was not excluded from bankruptcy mass, although this estate was introduced to these companies with former integrated-disintegrated processes mainly under political pressure,
- bankruptcy of cooperatives are generated without consultations with cooperative unions, so in the time between nominating bankruptcy manager till the ending of liquidation process – when all controller rights of cooperative members are suspended – sale of cooperative property were conducted on unreal low prices;
- cooperatives were eliminated as intermediary in the contracting process between agricultural producers as producers of raw materials and new-privatized companies in food industry;
- Foreign investments (EU, USA, Norway, Sweden, ...) and with technical assistance of number of foreign government agencies and NGOs,² new cooperatives organizations were set up using foreign donations with task to eliminate rural poverty, but that process were in number of cases without common outbreak of donors and existing cooperative unions. However, some cooperatives that emerged in this process we can rank in new generation of cooperatives and those are mainly specialized cooperatives of agricultural producers that are bigger market producers of vegetables and fruit.³
- Consumers cooperatives weren't ready for trade liberalisation and development of hypermarkets in countries in transition, which was manifested in Serbia with little delay;⁴

¹ In Serbia in 2002

² On revitalization of cooperative movement in Serbia were engaged American agencies IRD, ADF, CHF, VOCA and Mercy Crops (Economic revitalization of union); *Jaeren Produktutvikling* (Renewal of agricultural estates and cooperative by Norway model in Republic of Serbia), ...

³ Successful example of form NGC in Serbia is AGROCOOPERATIVA in Horgoš (Subotica region) that were founded vegetable producers with relatively high solitary share of 5.000 Euros and they built centre for finishing and packing of vegetables, with mutual sale to hypermarkets and other customers.

⁴ Due to disintegration of unique economic and political regime in ex SFR Yugoslavia (1990-1992), wars in surrounding territories (1991-1996), economic sanctions by UN State Council (1992-1996), NATO bombing (1999), ...

- Introducing institute „registered agricultural farm“ and their direct including in state subventions payment system, role of cooperatives were partly eliminated as their representative and intermediary in coordination of production-economic activities between cooperative members on one side and all other parties in agribusiness sector (food industry, trade, banks,...) with whom farmers used to do business through cooperative.

CONCLUSION

The NGC model is an outgrowth of the traditional agricultural business cooperative. Forces external to cooperatives (such as the industrialization of agriculture and globalization), and forces internal to cooperatives (free rider, horizon, and control problems) present significant challenges to the survival and success of traditional cooperatives. The NGC model may simply be an investment vehicle for the farmer, allowing the farmer to participate in the investment of his commodity beyond the farm gates. It has been argued that more extensive applications of the NGC model as potentially successful for attracting the necessary level of capitalisation to fund production process would require careful examination of the legal and taxation issues surrounding the use of delivery rights. It is also likely that initially the formation of NGC will be mainly based on niche markets and small scale investment opportunities.

Dominant characteristic of cooperative movement in transitional countries is that cooperatives inherited from socialistic period did not succeed to adapt in proper manner to fast changes during introducing of capitalistic way of production and significantly stronger competitiveness in processes of globalisation and liberalisation.

Adapting cooperative legislation to new changes in transitional countries were unstable and with results that are not completely according to international cooperative standards, nor they satisfy interest of cooperative members in some countries and activities.

Reform of cooperative movement in Serbia *de jure* has not even begun, because in seven years of political changes (2000) no new law on cooperatives were adopted, but in practise beside traditional agricultural cooperatives, some new cooperative organisation emerge. They represent new formed NGCs or former cooperatives that are trying to provide investment with higher shares and to transform themselves into NGCs.

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