



AgEcon SEARCH
RESEARCH IN AGRICULTURAL & APPLIED ECONOMICS

The World's Largest Open Access Agricultural & Applied Economics Digital Library

This document is discoverable and free to researchers across the globe due to the work of AgEcon Search.

Help ensure our sustainability.

Give to AgEcon Search

AgEcon Search

<http://ageconsearch.umn.edu>

aesearch@umn.edu

*Papers downloaded from **AgEcon Search** may be used for non-commercial purposes and personal study only. No other use, including posting to another Internet site, is permitted without permission from the copyright owner (not AgEcon Search), or as allowed under the provisions of Fair Use, U.S. Copyright Act, Title 17 U.S.C.*

Rural Supply and Marketing Cooperatives in China: Historical Development, Problems, and Reform

Xiangyu Guo, Todd M. Schmit, Brian M. Henehan*

Abstract

The historical development and performance of rural supply and marketing cooperatives (SMCs) in China are examined and linked to various reform periods. SMCs suffered a loss of focus on members as well as member control during several periods of reform and experienced declining financial performance during the most recent reform period. A number of factors related to this decline are presented, including ineffective reforms, lack of accountability and transparency, limited focus on member needs, a negative image for cooperatives, and poor understanding of contemporary cooperative management and governance practices.

Key words: China, economic reform, rural supply and marketing cooperatives

- * Xiangyu Guo is Professor, College of Economics and Management, Northeast Agricultural University, China and Visiting Scholar, Department of Applied Economics and Management, Cornell University, Todd M. Schmit (corresponding author; email tms1@cornell.edu) and Brian M. Henehan are Assistant Professor and Senior Extension Associate, respectively, Department of Applied Economics and Management, Cornell University, Ithaca, NY, USA.

Introduction

Given the scope of today's global market for food and agricultural products, there is a growing need to gain a better understanding of the impact of globalization and the world-wide outlook for food and agriculture. China is experiencing both increased demand for food products, as well as growth in the production of various farm and food products. However, rural communities and agricultural areas are not experiencing the economic growth and increases in per capita income that urban areas are.

Along with increasing production, is a paralleled increasing interest in organizational alternatives to increase the efficiency and operation of farm supply and food markets. In particular, recent reforms are encouraging the growth and development of member-driven cooperatives in China. As the rural and agricultural economy of China experiences significant change and the impact of government reform, there is a growing interest in adopting market driven business structures including new progressive, farmer-focused cooperative businesses.

Agricultural and rural cooperatives have experienced various challenges and changes, and the road of development has been full of twists and turns since the founding of the People's Republic of China (PRC) in 1949. However, the history and economic role of rural cooperatives in China has received limited attention in Western literature, particularly with respect to the changing structure of rural agricultural and food supply cooperatives following the most recent economic reforms.

Rural supply and marketing cooperatives (SMCs) are an important component of the planned economy system in China, particularly given their central roles in the procurement of rural farm commodities and the sales and distribution of agricultural inputs and retail consumer goods to rural households. However, SMC roles and activities over time have changed dramatically during various phases of reform and political ideologies, with particular consequences to the underlying farmer members. As such, a closer inspection of the historical development and potential growth opportunities for SMCs under current reform efforts is needed. Specifically, our objectives are to (i) describe the historical development and operations of rural SMCs in China and how the various phases of reform have impacted cooperative development and operations, (ii) review the current potential problems and challenges related to cooperative performance and success, and (iii) recommend strategies to enhance cooperative performance and successful new cooperative development.

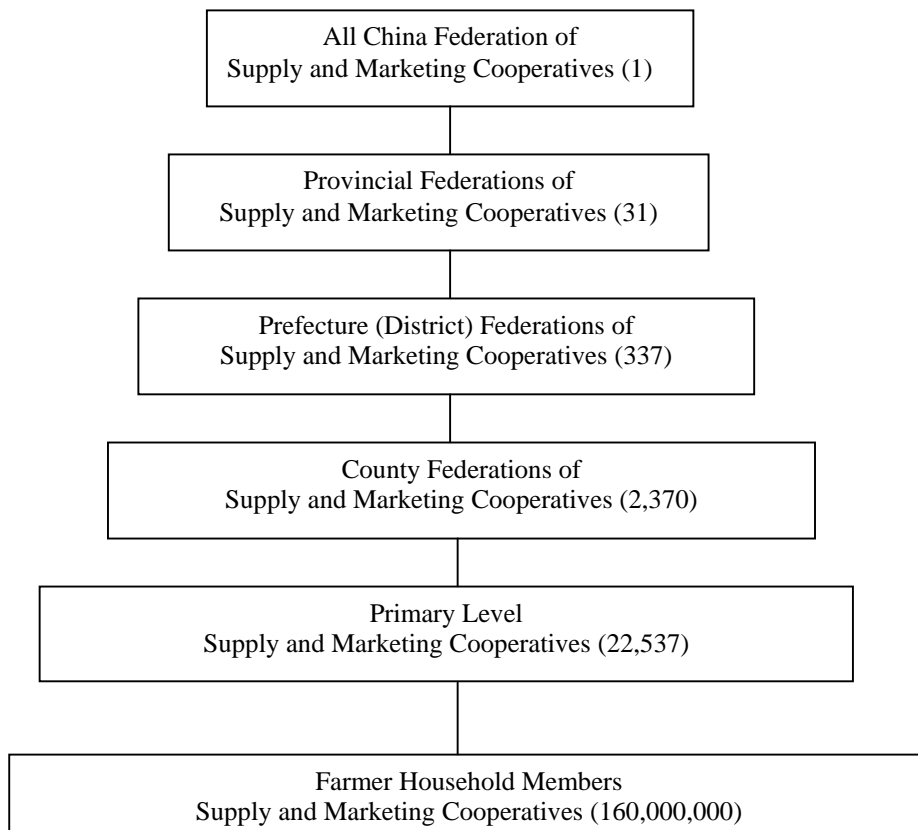
We continue now with a general discussion of the evolution of roles and activities of China's rural SMCs, followed by a more detailed discussion of SMC historical development across specific periods of change and/or reform. We then

highlight current problems and challenges to achieving successful SMC growth and close with some summary conclusions and recommendations, along with an outlook for cooperative reform.

SMC Evolution

Cooperative organizations with farmers as the main body are an important component of the rural economy. SMCs are part of a national, federated system housed within the All-China Federation of Supply and Marketing Cooperatives (AFSMC), with farmers as the principal members. Currently, the ACFSMC consists of one head office, 31 provincial branches, 337 prefecture (district) sub-branches, 2,370 county federations, and 22,537 primary societies (Figure 1). In total, this federation includes approximately 160 million rural households as its members and employs nearly 1.3 million people (AFSMC, 2008).

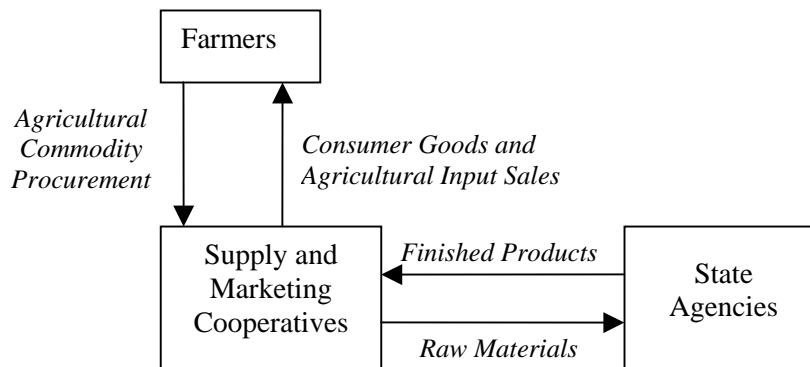
Figure 1. Organizational structure of supply and marketing cooperatives



The AFSMC organization is administered through its head office (e.g., administration, personnel, education, policy and economic development), but also includes several subordinate cooperative enterprises (e.g., industrial production, investment and property development, product development, foreign trade and commerce), commodity research institutes (e.g., fruits, tea, cotton, business machinery, resource recycling), subordinate organizations (e.g., cooperative media publications and communications, information center, science and technology), and industry associations and societies (e.g., food and commodity trade and marketing associations). Its functions are to guide SMC growth and reform, coordinate and manage SMC agricultural means of production under government authorization, maintain the legal rights of SMCs, coordinate commodity and product circulation between rural and urban areas, and to implement the policies of state councils on rural economic development (ACFSMC, 2008).

The success of achieving these functions is debatable and has certainly been influenced by changing political ideologies and directions of reform over time. In general, SMCs were originally collectively owned by farmer members with primary functions of procuring member products and providing back consumer goods and raw materials (Figure 2). SMCs received strong support for organization and development and their replacement of existing private enterprises monopolized the rural distribution system (Table 1). At that time, SMCs played an important role in promoting the interflow of goods between the cities and countryside, ensuring adequate market supplies, and accelerating the industrialized management of agriculture.

Figure 2. Original role of supply and marketing cooperatives in China



(Adapted from Tsang, 1994)

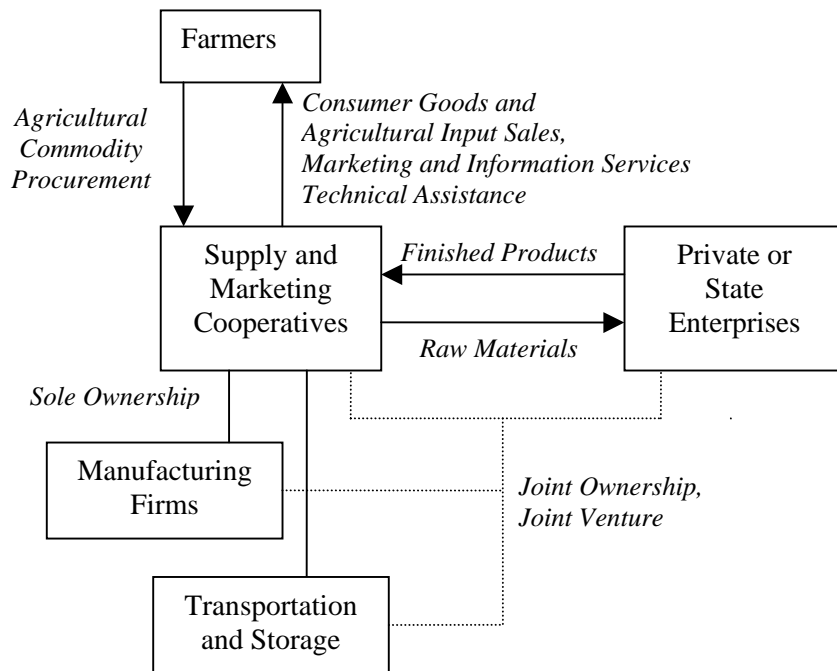
Table 1. Evolution of roles and functions of China supply and marketing cooperatives (SMCs).

Reform Period	SMC Functions and Developments	Rural Economic Conditions and Government Support
1949 – 1957 Growth and Success	<ul style="list-style-type: none"> • Collective ownership by peasants who subscribed shares • Dividends distributed • Member governance, boards of directors, supervising committees. • Grass-roots SMC establishment • Procured member products, sold consumer goods and raw materials 	<ul style="list-style-type: none"> • Government support for SMC organization and development. • Establishment of unitary system of SMCs nationwide (ACFSMC) • SMC strong growth, replaced existing private enterprises • Monopolized rural distribution system.
1958 -1982 Developmental Barriers	<ul style="list-style-type: none"> • Operated as state-owned enterprises of the government • Member governance structures and dividends abolished • State-administered pricing system • Procured member products, sold consumer goods and raw materials • Mismanagement, profiteering, and corruption by employees. 	<ul style="list-style-type: none"> • Change in political ideologies • Poor efficiency of SMCs, large agency costs, peasant grievances • People's communes abolished, producer land management rights established • Too few, distant SMCs limited peasant access to goods and sales. • Inadequate rural infrastructure, transportation, and storage facilities • Loss of ACFSMC individual identity or operations
1982 – Present Economic Reform	<ul style="list-style-type: none"> • Collective ownership renewed • Member participation in management encouraged • Full operational autonomy, employee incentive system restructured • Negotiated contract pricing for member products • Expanded scope of services in marketing, processing, storage, transport, technical guidance, wholesaling, and retailing • Joint ventures and collaborations with private rural enterprises in processing, distribution and storage 	<ul style="list-style-type: none"> • State coordinated efforts to expand functions of rural enterprises • ACFSMC reinstated as separate operating entity • More market-based system to increase competition from private enterprises and improve efficiency • Increased number of wholesale and retail market outlets • Strong growth in private sector market share and sales of peasant products to non-agricultural residents. • Different regulatory and reporting requirements for SMCs and private enterprises.

Before China's reform efforts in the 1980s, a change in political ideologies transformed SMCs into state-owned enterprises. While the SMCs served as an important tool with which the government controlled agriculture, rural areas, and farmers, member governance structures were abolished and mismanagement plagued the system. Poor operational efficiencies resulted with a depleted rural infrastructure, and inadequate facilities to serve rural farmers (Table 1). The ACFSMC lost its individual identity and became amalgamated within other state agencies.

Under current reform efforts, collective ownership is being renewed and the ACFSMC has been reinstated as a separate operating entity (Table 1). The roles of SMCs are changing rapidly, but reform progress has been far from smooth. SMC roles have expanded into product manufacturing, market information and technical assistance services, and coordinated transportation and storage activities (Figure 3). However, in order to instill a more market-based system, state efforts have encouraged competition with expanded functions of rural (private) enterprises. As a result, SMCs gradually lost their traditional superiority given strong growth in the private sector and eroding SMC market shares (Tsang, 1994).

Figure 3. Evolved role of supply and marketing cooperatives in China



(Adapted from Tsang, 1994)

Reform efforts have been limited by complex and confusing allocations of property rights, lost emphasis on 'real' farmer cooperative principles and ownership, and vague SMC positioning and misleading policies (Shen, 2004; Yang, 2003; Xu and Huang, 2006). The results are evident in the difficulty that remains in re-establishing strong links with farmers and poor overall performance. While the introduction to a more market-based economy increased the number of wholesale and retail outlets and opportunities for collaborations with private firms, the operational opportunities and regulatory environments under which entities operate appear uneven, putting SMCs at a competitive disadvantage (Tsang, 2004).

SMC Historical Development

The history of China's SMCs can be divided into three main periods: the success and growth period (1949 – 1957), the erratic and slow development period (1958 – 1981), and the reform period (1982 – present). A summary of generally accepted cooperative principles is given in Table 2, along with the relevance to China's SMCs operational characteristics in each defined period. These items are discussed more specifically below.

SMC Success and Growth

At the beginning of the Republic, from 1949 to 1957, SMCs developed smoothly and successfully. In November, 1949, the Central People's Government (CPG) of the PRCC set up the State Administration of Cooperative Business (SACB) with responsibility for organization, guidance, and promotion of the development of supply and marketing, consumer, credit, transportation, fishery, and handicraft industry cooperatives for the country. By the following July, SACB held the first national meeting of cooperative staff, at which the United Headquarters of Chinese Cooperatives was created and took charge in leading and developing cooperatives.

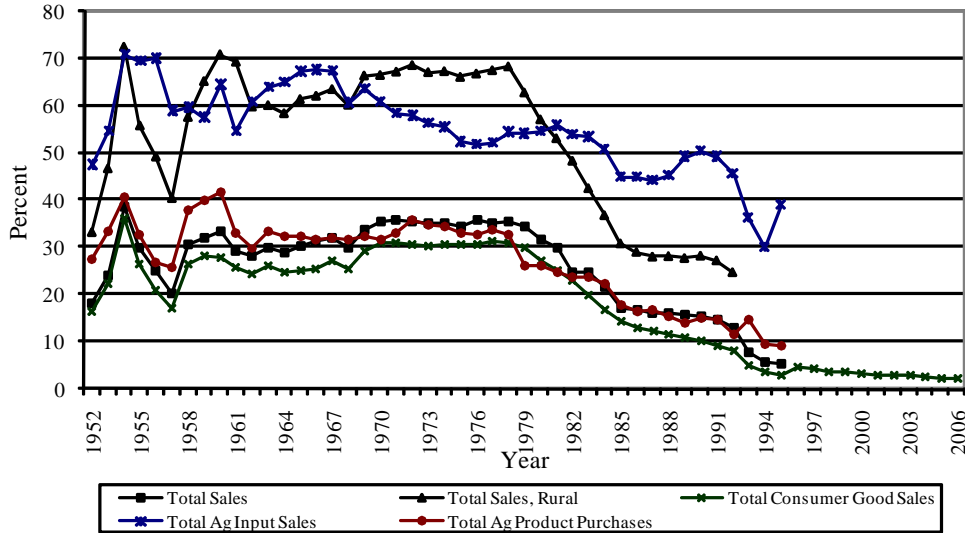
In July 1954, the first national member congress of cooperatives was convened under a new name, the All-China Federation of Supply and Marketing Cooperatives (ACFSMC), and set up a unitary system of SMCs nationwide. Cooperative leading bodies were established at all levels, from the top down, and a national organizational system took shape. At the same time, individual SMC organizations were established at all levels, from the bottom up, and an independent, unitary, and comprehensive SMC system was completed. By the end of 1957, the number of primary societies of SMCs was 19,402 with over 157 million members (30 percent of the rural population) that subscribed shares, and employed 1.68 million people (National Bureau of Statistics).

Table 2. Operational and governance characteristics of supply and marketing cooperatives (SMCs).

Cooperative Characteristic	Growth and Success 1949-1957	Developmental Barriers 1958-1981	Economic Reform 1982-Present
Member Control:			
• Participation in meetings	Participated	None	Few SMCs
• Voting	Voting rights	None	Few SMCs
Board of Directors:			
• Majority government appointees	No Member elected	All None	SMCs appoint SMCs appoint
• Majority member elected			
Property Rights:			
• Members can own equity	Yes	No	Less
• Members can redeem equity	Yes	No	No
Earnings Distribution:			
• Members can receive	Yes	No	Few SMCs
• Earnings go to government	No	All	All
Independent Management:			
• Accountable to members	Yes	No	Few SMCs
Transparency:			
• Member access to financial and operating data	Yes	No	Few SMCs
• Receive annual/quarterly reports	More	No	Few SMCs
Legal or Statutory Requirements:			
• Director or manager liability	Yes	No	No
• Member rights	Yes	No	No
• Outside accounting audits	Yes	No	No

During this period, the mission of SMCs was to serve agricultural producers and to expand agricultural business. As a result, SMCs played a dominant position in the rural market and evolved into the main channel of commodity circulation. In 1957, the total purchase of farm products by SMCs amounted to 5.61 billion yuan, accounting for 26% of the total farm products sold by farmers. Total retail sales of commodities amounted to 9.51 billion yuan (in nominal terms), or 20% of the total retail sales in 1957, and 40% of the retail sales in rural areas (Figure 4). Inclusive in that amount were sales of agricultural inputs of 1.92 billion yuan, or 59% of the total agricultural inputs in China (National Bureau of Statistics).

Figure 4. Supply and marketing cooperative (SMC) market shares of sales of consumer goods and agricultural inputs and purchases of farm products



Compiled from: *China Statistical Yearbook*, *China Domestic Trade Yearbook*, *China Business Yearbook*, and *Statistics of China Supply and Marketing Cooperatives*, various issues.

Several factors influenced the vigorous and healthy development of SMCs during this period. First, the developmental needs of rural commodity economies were internal forces causing SMCs to emerge and develop rapidly. In addition, direct government participation and support provided the external infrastructure essential for the establishment and development of SMCs (Table 1). The government promoted development of the SMCs by means of legal protection, economic support, and technical direction. In 1950, the *Cooperative Law of People's Republic of China* was approved. In 1954, the *Bylaws of the All-China Federation of Supply and Marketing Cooperatives* were passed and, at the same time, the government gave SMCs financial, tax, and credit support. Later that year, the *Demonstration Bylaws of the Grass Root Supply and Marketing Cooperative* was made known and carried out. The central and local governments appropriated funds to new SMCs, and SMCs were free of income taxes for the first year. The lending rate of state banks to SMCs was discounted 10% below state-run commerce.

The commitment of SMCs to operate under the mission of serving farmer-members was an important and essential condition that supported the development and growth of SMCs. Adhering to collective ownership was the prerequisite for the existence and smooth development of SMCs. Implementing and steadily

improving the system of democratic member control was the basic governance guarantee to promote vigorous development during this period (Table 2). SMCs adhered to the system of the member congress, the ACFSMC, and the National Committee of the ACFSMC was elected at the first national congress in 1954. The Committee acted on their behalf, and conferred three additional conferences in 1955, 1956, and 1957. At the same time, SMCs improved the roles of the council board of directors and supervising committees.

SMC Developmental Barriers

From 1958 to 1981, SMCs entered a long period of slow development due largely to changes in political ideologies. During this period, SMCs were reorganized as state-run commerce where collective ownership was replaced by ownership of the entire people (Table 1). SMCs deviated from the concept and principles of cooperatives, such as user-control and user benefits, and subsequently sustained historic losses.

In 1958, the ACFSMC and the Urban Service Department were amalgamated by the State Council and renamed as the Second Ministry of Commerce and SMCs changed into predominantly a business administrative organization of the government at all levels. SMC businesses were placed under the control of the state-owned commercial sectors, and member-governance operational structures, such as member meetings and boards of directors, were abolished (Table 2). The cooperatives remained in name, but were actually operated by the Ministry of Commerce as public firms (Yao, 1985).

A departure from the aim of serving its members brought setbacks to SMCs. However, the Central Committee of the Communist Party of China decided to re-focus on SMCs in 1961 and in 1962 reestablished the ACFSMC as a separate operating entity. At this time new development of SMCs occurred and by the end of 1962, there were 25 provinces, 176 prefectures, and 2,042 counties that had functioning SMCs, and the primary societies returned to the SMC system (National Bureau of Statistics).

The re-focusing on SMCs and the separate identity of the ACFSMC in 1962 was, unfortunately, short-lived. SMCs were criticized politically as something similar to the capitalistic and revisionist efforts that occurred during the Great Cultural Revolution and the *Demonstration Bylaws of the Grass Root Supply and Marketing Cooperative* were abolished in 1966. By 1970, the ACFSMC was combined with the Ministry of Commerce, the Ministry of Food, and the Bureau of Industry and Commerce Administration and the national system of SMCs was merged with state-run commerce. SMCs once again lost their right of independent decision making and were required to turn in their profits to the Ministry of Finance. As a result, SMCs suffered significant losses of capital and equity.

While the SMCs still existed in name, they were no longer farmer-owned and managed organizations (Table 2).

In the face of rural criticism and in order to strengthen rural commerce and improve relations with farmers, the ACFSMC was once again reestablished as a separate entity in 1975, but was still, in reality, within the Ministry of Commerce in rural areas and a department of the States Council. After the Third Plenary Session of the 11th CPC Central Committee that reformed the rural economic system in 1978, the system of the people's commune was abolished and farmers became independent producers. They began to have rights to manage their lands, but they were in need of access to additional agricultural inputs and increased opportunities to sell their products.

Although farmers' economic activity increased, the market share of SMCs descended due to abuse of the management system and other problems. Between 1974 and 1981, the SMC's market share of total retail sales decreased by over 5 percentage points, and in rural areas dropped over 14 percentage points (Figure 4). In addition, the SMC's market share of the purchase of farm products sold by farmers declined nearly 10 percentage points (National Bureau of Statistics).

A number of conclusions can be drawn from this period that resulted in poor economic performance for SMCs and farmer members, and a distrust of the traditional SMC system. The establishment of the planned economy, in particular, undermined SMCs' ability to own property. The abolition of existing organizational systems within SMCs was a direct obstacle to its aim of serving members. A lack of legal and statutory protection and excessive government intervention resulted in the SMCs merging with the state-run commerce. As a result, limited accountability and transparency resulted in less effective management and governance (Table 2).

SMC Reform Period

Entering the 1980s, with the arrival of rural economic reform, SMCs were facing rigorous challenges. In addition, SMCs began losing their traditional dominant role in rural agriculture due to the dramatic development of the country's market economy. These changes created challenges for the development of the rural economy and for meeting the needs of farmers. As a result, China began renewed SMC reform efforts in 1982 (Table 1). The course of this recent reform can be divided into five phases as described below.

In phase one (1982-1983), the main focus was to restore the primary operational characteristics of SMCs; i.e., collective ownership and member participation, flexibility in operation, and democracy in management. By the end of 1983, over 91% of primary societies of SMCs had redesigned management operations, enlarged cooperative equities, and developed new members. The

number of farmers who had bought shares and became members reached 130 million, less than that in the early success period due to reduced rural populations, but accounted for over 70% of all farmers (National Bureau of Statistics).

In phase two (1984-1985), the emphasis was on SMC and market system adjustments. In particular efforts were prioritized to: (i) lessen restrictions on farmers' purchasing shares, (ii) expand the scope of cooperative operations and services, (iii) improve the effectiveness and operations of the employment and personnel system, (iv) improve and better develop the food and agricultural distribution system, and (v) and address the inequities of the price administration system. The scope of SMCs expanded to include processing, storage, transportation, and technical guidance. SMC purchases of agricultural products were mostly done on a contractual/negotiated basis with the member, rather than on a state-administered price basis.

The strong growth in private rural enterprises provided opportunities for SMCs to assist them with marketing, sourcing, and providing market information. SMCs established several wholesale markets to connect buyers and sellers and increased the number of outlets for supply of raw materials and consumer goods to rural areas (Tsang, 1994). By late 1985, farmer equities and funds raised reached 2.2 billion yuan in nominal terms, six times above the level in 1981, prior to the SMC reforms (National Bureau of Statistics).

In phase three (1986-1994), reform efforts centered on the development, improvement, and integration of agricultural-based economic industries. Specifically, efforts were focused on developing services for commercial production, crosswise economic affiliations, and agricultural product processing industries. These efforts would be supported by the development of alternative operational forms of business and management, rural commercial networks, and educational, scientific, and technical undertakings. SMCs realized full autonomy in sourcing supplies rather than restricted to state enterprise purchases (Tsang 1994). In addition, some SMCs established their own processing facilities, and many formed joint ownership or joint venture agreements with new private rural enterprises (Figure 4).

Agri-technology services were provided to peasants, often joint with universities on crop diseases, new crop species, and related technical information. By 1987, the purchase sum of agricultural products of SMCs reached 39.5 billion yuan (nominal), an increase of nearly 32% over 1985, and retail sales of 93.6 billion yuan (nominal) were up 28% (National Bureau of Statistics). Later efforts in this period were largely tasked to deepen and improve the former contents of the reform.

In phase four (1995-2001), the central authorities identified and prioritized the deepening reform of SMCs as a major and pressing task. Early in 1995, the CPC

Central Committee and the States Council issued the *Decision about Deepening Reform of Supply and Marketing Cooperatives*. The aim of which was to reform SMCs into viable farmer cooperative economic organizations by rationalizing the current organizational system to rural farmers, strengthening SMC service functions, improving operational mechanisms, intensifying supervision and management, and offering additional protection and support to SMCs. In May of that year, the second National Congress of China's SMCs was held. Efforts continued to encourage member participation in SMC management and dissemination of agricultural market and price information to members and (non-member) rural enterprises became a primary service provided (Tsang, 1994)

In the current phase (2002-present), the ACFSMC is concentrating on improving economic operations and performance of SMCs and has put forth additional reform policies. Specifically, they are working to restructure primary societies aimed at industrialized management of agriculture, modernizing cooperative enterprises by allowing multiple property rights, recreating federations of cooperatives by adjoining cooperatives with subordinate cooperative enterprises, and rebuilding business networks by developing modern management practices. County-level SMCs no longer serve as a supervising body, but as a federation of grassroots cooperatives. Restructuring the employee incentive system to reduce opportunities for corruption was also a high priority, as well as increasing business linkages with both rural enterprises and urban economies.

Current Problems and Challenges

Arguably, the reform of SMCs has achieved some success. Xu and Wang (2006) report that in 2005, the aggregate system of SMCs had assets in excess of 46 billion yuan (nominal), 160 million members, and 1.3 million employees. In 2006, gross sales of nearly 750 billion yuan and profits of nearly 8 billion yuan were reported, a nearly a five-fold increase from 2000 (Bai 2007). At the same time, however, SMCs continue to face many problems and challenges. According to Zhang (2003), the reform of SMCs has not been successful due to ownership worship that hinders reform efforts, current policies that mislead reform, and confusing and imperfect allocation of property rights that limits effective reform.

Member Operation and Service

The most fundamental problem is that many existing SMCs are not structured or operated on a member-driven cooperatives basis and are not truly owned by farmer-members. While collective ownership was renewed under current reform efforts and member participation is being encouraged, the relationship between the

SMCs and farmers hasn't improved materially and the status of farmer-members as cooperative owners has not been accurately reflected (Shen 2004). The underlying purpose in serving its members has not been fully implemented and accomplished. Under the current market economy, the supply of new agricultural production and marketing services is most needed but has not been addressed fully by SMCs. Since the current reform efforts began, SMCs have not sufficiently differentiated its members from non-members.

Current SMCs are not following cooperative principles, principally by not operating under the democratic control of its farmer-members. Unfortunately, the national congress of ACFSMC appears to be more of a formality than a driving force in cooperative reform. While the national congress reconvened in 1995 after a 41 year absence, it was attended by only 51 farmer representatives, only 7% of the total (*China SMC Review*, 1995). More than 90% of those attending were directors of boards of primary societies and other federation levels of SMCs and managers of subordinate cooperative enterprises - representatives appointed by the government and not elected by their members,.

Financial Performance

SMCs continue to face many economic difficulties and poor operating. One of the prominent problems has been a historically heavy debt load. A debt load of more than 20 billion yuan (nominal) in 1995 has resulted in large interest payment burdens (Guo et al., 1999). Large operating deficits are another problem. The aggregate system of national SMCs experienced losses for eight consecutive years from 1992 through 1999. A loss of 4 billion yuan in 1994 amounted to over 5% per cent of SMC's own funds. Losses topped 70 billion yuan in 1997 and nearly 13 billion yuan (nominal) in 1999 (National Bureau of Statistics).

Heavy debt loads and operating losses contributed to large reductions in SMC net returns. The rate of return on investment (ROI) declined from 25% in 1949 to only 10% in 1957. ROI continued declining from 8% to 5% during the difficult development period of 1958 - 1981, and further declined to around 4% after the reform period of 1982 -1988 (Guo et al., 1999).

SMC's market share of consumer goods sales, the predominant sales category, has also declined considerably. In 1971, SMC market share was relatively high at over 31%, but since then, SMC market share has shown a precipitous decline (Figure 4). Retail sales of consumer goods by SMCs in 1992 accounted for just over an 8% market share, the year before the latest SMC reform period started. Retail sales of consumer goods of SMCs, however, continued to decline and in 2006 accounted for just over a 2% market share (Figure 4).

Along with the decline in market share of consumer goods sales, SMC's shares of agricultural input sales and the purchase of farm products have also declined

substantially since 1971. The retail sales of agricultural inputs by SMCs in 1992 accounted for a 46% market share of total retail sales, down 13 percentage points since 1971 and 10 percentage points since 1981 (Figure 4). While the proportion of agricultural input sales appears to have grown somewhat in 1995, from 30% to 40% from 1994, more recent data is unavailable to see if this trend has continued. However, this may be a reflection of the increase in market and price information services and other technical assistance provided.

The purchase of farm products by SMCs in 1992 accounted for only a 12% market share of total farm products sold by farmers, down 22 and 13 percentage points since 1971 and 1981, respectively. By 1995, the last year for which data is available, this share has dropped to only 9% (Figure 4), and continues to follow the trend retail sales to farmers quite closely. Retail sales of consumer goods and agricultural production inputs by SMCs were the major player in rural areas for much of their history, with market shares consistently near 70% for much of the pre-reform period. This traditional role, as discussed above, has been diminished greatly. By 1992, the share of total retail sales in rural areas by SMCs was below 25%. With more recent attention towards joint ventures and relationships with private enterprises in rural areas, it will be interesting to see with more recent data if this trend has continued post-1992.

Knowledge of Contemporary Management and Governance

While recent reform efforts have sought to re-establish and strengthen SMCs and their cooperative principles, many leaders in these organizations are lacking the knowledge of contemporary cooperative management and governance. This is an ideological obstacle to the further reform and success of SMCs. Up to now, in the course of SMC's reform, many managers and employees were unfamiliar with how contemporary cooperatives are governed and administered effectively. As such, they have not gained a sufficient understanding of the policies relating to SMC reform put forth by the Central Committee of the CPC and the State Council and, therefore, have difficulty in implementing reform effectively.

Managers, members, and employees are having difficulty in addressing this knowledge gap. Vast numbers of farmer-members are not only short of knowledge about cooperatives but go so far as to misinterpret cooperative principles. As a result, their participation in the democratic control of SMC is limited. A major challenge facing SMCs is gaining a better understanding of their role as a distinct institutional arrangement, namely its necessity and potential as a successful cooperative contributing to the economic development of rural China.

Conclusions

As recent reforms begun in 2002 continue to unfold, there is an increased emphasis on reconstructing primary cooperative societies to allow for separate cooperative enterprises that encourage modern management approaches and multiple property rights of members. Reform has achieved some success; however, a significant number of SMCs face ongoing operating losses and heavy debt loads. Reform is advancing at a slow rate and the farm economy is failing to keep up with the rest of the Chinese economy.

On the whole, cooperatives have three current options for furthering SMC reform; i.e., they must take on the responsibility of either (1) becoming primarily oriented to agriculture, rural areas, and farmers, (2) becoming oriented as an administrative institution, or (3) becoming oriented to particular enterprises or market functions. The first orientation is the most realistic and feasible compared to the other two. However, moving towards a stronger orientation to agriculture, rural areas, and farmers is difficult, requiring the cooperative to undergo further and deeper reforms and restructuring aimed at addressing the fundamental problems that the cooperative faces. In other words, the key link to reform is how to identify the proper ultimate owners and to establish an effective governance structure. In addition, the absence of ultimate owners can result in insiders' domination over residual claims (Xu and Huang, 2006)

To deepen the reform of SMCs, a process enjoined with the complementary needs of rural economic development may accelerate an increase in the income of farmer-members, bring about improvements to their living conditions, and raise their social and economic status. Considering the establishment of a defined system in which property and distribution of returns are subject to the democratic control of farmer-members will encourage farmers and SMCs to organize accordingly in response to market conditions. Continued support of existing and new SMCs in China is needed to enhance their formation, viability, and development.

There are a number of challenges in educating cooperative managers, members, farmer-leaders and policy makers on the cooperative business model. The principles and practices of member-oriented cooperative enterprises can be misunderstood and misinterpreted which can result in creating a negative image for cooperatives (see e.g., Anderson and Henehan, 2005). This negative image can deter farmers from joining or remaining loyal to cooperatives, and undermine the confidence among policy makers in the cooperative business model.

The development of educational programs is needed on contemporary cooperative administration and governance practices for key decision makers. Research focusing on developing a better understanding of why SMCs are performing poorly could assist in the development of educational tools aimed at

improving SMC performance. The analysis of individual SMC performance and correlation with data on cooperative management performance and effective governance could be used for creating benchmarks for use by cooperative managers and leaders.

Increased resources should be made available for applied research and educational efforts aimed at better understanding and implementing a more contemporary cooperative business model in rural China. Deeper reform of the cooperative sector might better accommodate member ownership, member-control, and more member-driven governance structures. A more member-driven cooperative system could yield better economic results in stimulating the rural economy.

References

- All China Federation of Supply and Marketing Cooperatives, ACFSMC (2007). Online access, www.acfsmc.cn.
- Anderson, B.L. and B. Henehan (2005). "What Gives Agricultural Co-operatives a Bad Name?" *International Journal of Co-operative Management* 2, 9–15.
- Bai, L. (2007). "Searching after the Road of the Development of the Supply and Marketing Cooperatives under the Market Economy." *China Co-Operation Economy* 6, 10–15. (Chinese)
- China SMC Review* (1995). "Representatives of the 1995 All-China Federation of Supply and Marketing Cooperative Congress." *China Supply and Marketing Cooperative Review* 6, 15.
- Guo, X., P. Sun, and Z. Qiumei (1999). "The Plight and its Courses Facing the Supply and Marketing Cooperatives in China." *Commercial Research* 5, 63–65. (Chinese)
- National Bureau of Statistics. (1989–1993) *China Statistical Yearbook*. Beijing: China Statistics Press, various issues. (Chinese)
- National Bureau of Statistics. (2001–2002) *China Domestic Trade Yearbook*. Beijing: China Economic Press. (Chinese)
- National Bureau of Statistics. (1991–2006) *China Business Yearbook*. Beijing: China Commerce and Trade Press, various issues. (Chinese)
- National Bureau of Statistics. (1986) *Selected Historical Materials of China's Supply and Marketing Cooperatives*. v. 1. Beijing: China Financial and Economic Press. (Chinese)
- National Bureau of Statistics. (1994) *Selected Historical Materials of China's Supply and Marketing Cooperatives*. v. 4. Beijing: China Financial and Economic Press. (Chinese)

- National Bureau of Statistics. (1949–1988) *Statistics of China Supply and Marketing Cooperatives*. Beijing: China Statistics Press, various issues. (Chinese)
- Shen, L. (2004). “The End and Rebirth of an Important Economic Organization.” *Journal of Kunming University of Science and Technology* 4, 37–39. (Chinese)
- Tsang, E.W.K. (1994). “The Changing Role of Supply and Marketing Cooperatives in China.” *Small Enterprise Development*. 5, 35–42.
- Xu, X. and Z. Huang (2006). “Supply and Marketing Cooperatives in Institutional Transition - Problems, Property Rights and Tendencies.” *Journal of Zhejiang University (Humanities and Social Sciences)* 36, 117–124. (Chinese)
- Yang, Z. (2003). “Research on Reform Goal of the China Supply & Marketing Cooperatives.” *Problem of Agricultural Economy* 6, 56–60. (Chinese)
- Yao, X. (1985). “The Reform of Agricultural Marketing and Supply Cooperatives in China.” M.S. Thesis. Michigan State University, Lansing, MI.
- Zhang, S. (2003). “The Reform of Supply & Marketing Cooperatives: Crux, Misunderstanding and Dilemma” *Journal of Finance and Economics, Shanxi University* 25, 27–30. (Chinese)