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E. G. Nourse's Place in Contemporary Cooperative Theory and Practice

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As early as 1922 E. G. Nourse contributed to the economic theory of cooperation. The 1945 article, "The Place of the Cooperative in our National Economy," reprinted here states concisely and clearly Nourse's argument for a limited cooperative role in the economy. This preference for a limited role was not entirely predicated upon the cooperative business form itself. Rather, it is a specific application of Nourse's more general conviction, as an adherent of the "old" Chicago school, that no firm should be so large that it can individually, or in concert with others, cartelize a market (Simons).

In Nourse's words, no firm should become a "commercial Napoleon." Nourse wanted cooperatives, chips fall where they may, to make markets more competitive to enhance economic efficiency. Within his analysis, cooperatives have a clear-cut role to play where farmers are the victims of monopoly power in input markets or monopsony power in output markets. Using the cooperative business form farmers should enter such markets with sufficient capacity to force established firms to raise (lower) prices paid for farm outputs (inputs). Benefits thereby accrue not only to patron-owners but to all farmers who use the market. Having just completed major studies at the Brookings Institution on industrial pricing practices, Nourse was convinced that farmer cooperatives should operate "pilot plants" in this fashion to steer markets to harbors of maximum social benefit for farmers and the general consuming public.

This fundamental insight obviously continues to be relevant today. Farmer cooperatives that successfully enter, or as Nourse pointed out, credibly threaten to enter a noncompetitive input supply or downstream food marketing industry can improve the welfare position of producers. However, advances in cooperative theory and the conduct of particular types of cooperatives since Nourse's era have demonstrated that this competitive yardstick outcome is only one of several performance possibilities. Moreover, it may not be the most salutary outcome for cooperative survival.

Implicit in Nourse's yardstick theory is a free rider problem that cooperatives have not easily been able to solve. All farmers in the market benefit, however, only members bear the costs, including capital investment and

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oversight costs, necessary for successful yardstick operations. Helmberger and Youde and Helmberger first demonstrated that closed membership cooperatives internalize the benefits of cooperation but do not have a yardstick effect on other firms in their market. Cotterill (1987) similarly established that a cooperative's financial structure and related surplus allocation practices determine the extent to which a cooperative has a yardstick effect on oligopolistic rivals. A cooperative, for example, that operates in a tight oligopoly and retains all shared monopoly earnings rather than allocating them to members does not disturb the oligopoly equilibrium. Since members and, more important, potential members receive no economic benefit relative to purchasing at the investor-owned firms, the IOFs are not forced to lower price to prevent customers from shifting to the cooperative.

Cooperatives that accumulate sizable unallocated retained earnings by being "good corporate citizens" in noncompetitive industries can develop organizational slack—preferring the quiet life of business as usual rather than the aggressive pursuit of new opportunities, cost controls, new technologies, etc. On the other hand, what major cooperative during the agricultural depression of the 1980s would not have loved to have been blessed with a major portion of their assets financed by unallocated retained earnings? Notwithstanding the agency problems related to unallocated retained earnings, financial stability of a cooperative may come as a trade-off to the vigor with which it performs its yardstick role.

Nourse's other main point is his clear-cut aversion to using a cooperative to cartelize the supply of an agricultural product. He wanted cooperatives to eschew monopolistic practices in their quest for improved economic welfare for farmers. Like most economists of his time Nourse saw little redeeming economic value in cartels. Their prominent role in the fascist economics of the interwar period convinced Nourse and others that cartelized industries are not compatible with democracy.

Nourse's ideas on cartelization often surfaced as one side in the famous debate with Aaron Sapiro and his commodity marketing school of cooperative action. The "eight commandments" that Sapiro preached to farmers included the use of long term, binding contracts to pool grower's product, marketing in common by a single agency according to grade and product quality, and control of a sufficient proportion of the entire crop to be a dominant factor in the market.

As I have argued elsewhere, Sapiro was not a promoter of coercive power through cooperative cartels (Cotterill 1984). He was a disciple of Bernard M. Baruch, one of the most influential thinkers of his generation. Baruch was convinced that men in government and industry should plan economic activity. Market forces had to be channeled by large-scale public and private organizations to improve human welfare (Baruch). Berle and Means and John Kenneth Galbraith subsequently elaborated Baruch's preference for the "visible" hand into theories on the separation of ownership from control, the industrial state, and the technocracy. In the 1930s laissez faire "market forces" understandably were not very popular, and the New Deal ushered in a broad array of public or quasi-public agencies and policies that opened up the middle road of mixed capitalization as an alternative to the extremist political systems of fascism and communism with their monopolistic economic systems.

In agriculture during the 1930s the dilemma was how to plan and control production in the agricultural sector without sacrificing the individual freedom so central to American political and economic philosophy. Also, how could production control avoid Nourse's fear of the loss of a reasonably priced food supply for consumers? The Agricultural Adjustment Act of 1933 diffused these concerns by authorizing the federal government to control production in a unique way. The method, now well known and accepted, was revolutionary at the time. The government would pay farmers who *voluntarily agreed* not to plant. It would set their payment level high enough to attract the amount of voluntary compliance needed to constrain production to the desired level. Farmer's freedom of choice was preserved. Exhorting cooperation was not necessary, and production was curtailed to a level that balanced the public interest with the special interests of farmers.

Arthur Schlesinger, the preeminent historian of the New Deal, elaborates:

> Here was democracy's feasible middle way between a self interest which meant anarchy and a coercion which meant tyranny—planning by incentive, rather than planning by command. (p. 72)

The New Deal's reordering of private incentives and public power continues to be of great importance to cooperatives. Since 1933 cooperatives have not been charged with the burden of attempting to restore balance to the economy. The government is charged with maintaining parity for agriculture as a sector. Cooperatives now focus their efforts on the two aspects of the farm problem that they are most suited to solve, the short-run stabilization issue and the need for efficient and easily accessed market channels for the family farm. Nourse's understanding of the benefits and limits of cooperation was validated by the reforms of the New Deal.

Today the indiscriminate dismantling of all New Deal agricultural institutions and policies is a plank in some political platforms. Before we do revert to a "free" market agriculture, one has to answer two questions affirmatively. Have agricultural markets lost their unique features compared with industrial markets? Are cooperatives better positioned today to assume an expanded responsibility for orderly marketing than they were in the 1920s and 1930s? In my opinion the answer of Nourse and his generation still stands. The American agricultural success story owes more to the complex institutional structure forged in the crucible of economic and political hardship during the first half of the twentieth century than current would-be radical reformers recognize. Today the challenge is how to retain the balancing properties of the middle road approach in this country while harmonizing it with the systems of other countries.

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